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Byron D. Sher

Alan R. Bromberg

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TEXAS PARTNERSHIP LAW IN THE 20TH CENTURY — WHY TEXAS SHOULD ADOPT THE UNIFORM PARTNERSHIP ACT

by

Byron D. Sber and Alan R. Bromberg†*

IN 1955, Texas took two significant forward steps in the long-needed modernization of the law governing business associations in this state. In that year, the Legislature enacted the Uniform Limited Partnership Act¹ and the new Texas Business Corporation Act.² In the field of general partnership law, however, Texas still lags behind most states, and its attorneys and businessmen are plagued by an uncertain and, in a number of respects, deficient body of law, which could be vastly improved by the adoption of the Uniform Partnership Act.³

At the time of its approval of the act in 1914, The National Conference of Commissioners on Uniform State Laws advanced as reasons in support of its recommendation for adoption of the act the lack of uniformity of the law among the states and its desirability because of the increasing number of partnerships carrying on business in more than one state and having as members residents of different states; the uncertainty in the existing law of partnerships due to conflict of decisions of different states and lack of consistency in legal theory; and the scarcity or absence of authority on important matters in the conduct and winding up of partnership affairs.⁴ These reasons are, if anything, even

* B.S., Washington University; LL.B., Harvard University; former Assistant Professor of Law, Southern Methodist University; Assistant Professor of Law, Stanford University.

† A.B., Harvard University; LL.B., Yale University; Associate Professor of Law, Southern Methodist University. Professor Bromberg expresses his appreciation to Eugene L. Smith for assistance in the preparation of his part of this Article.

¹ Tex. Rev. Civ. Stat. Ann. art. 6132a (1956 Supp.).

² Tex. Bus. Corp. Act Ann. (1956).

³ 7 Uniform Laws Ann. §§ 1-45 (1949). The Uniform Partnership Act is set out in full in the Appendix, *infra* p. 319; it will be referred to as the "act" throughout this Article. The Commissioners' Notes appear after each section in Uniform Partnership Act Ann.; they will be cited hereafter as "Commissioners' Note" with a reference to the appropriate section.

⁴ Commissioners' Prefatory Note, Uniform Partnership Act Ann. 1 (1949).

more appealing today.⁵ But wholly apart from these considerations, there are a number of positive defects in the Texas law which, together with the areas of uncertainty, it is the purpose of this Article to point out in an effort to enlist support for the enactment of the Uniform Partnership Act in Texas.

I. THE EXISTENCE OF A PARTNERSHIP

The Texas courts, like those of every other state, have frequently struggled with the question of whether or not a particular business association is a partnership. The question most often arises when a creditor seeks to collect a claim from one alleged to be a partner of the person with whom the creditor dealt in extending credit and who is thus liable for the debt.⁶

In some of the early cases there were indications that the Texas courts might follow the old English test of the existence of a partnership, long since repudiated,⁷ that the mere participation in profits of a business makes the participant a partner.⁸ The basis of the "profit-sharing" or "net profit" test is that fairness requires that one who shares in the profits of a business should be liable for the obligations incurred in carrying on that business. The test is defective, however, in that it fails to recognize that it is very common in business arrangements for a percentage of the profits of a business to be used as a convenient device for measuring such things as interest on a loan or rent, and that the lender or the landlord is not participating in the profits as an owner of

⁵ The act has been adopted by thirty-five states, Alaska and Guam. Table Of States Wherein Act Has Been Adopted, Uniform Partnership Act Ann. 6 (1956 Supp.). That the act has proved itself and is as appealing today as when it was enacted is attested to by the fact that it has been adopted in seven states since 1950. *Ibid.* Thus, by adopting the act, Texas could achieve uniformity of partnership law with three fourths of the states; moreover, it would not be acting blindly because of the many cases in those states interpreting various sections of the act, which become a part of any system of uniform laws.

⁶ *Crane, Partnership* § 4 (2d ed. 1952). However, the question of whether there is a partnership is by no means limited to the liability-for-debts situation. See, e.g., *Millers' Indemnity Underwriters v. Patten*, 238 S.W. 240 (Tex. Civ. App. 1922), *aff'd*, 250 S.W. 154 (Tex. Comm. App. 1923) (question of whether man was a partner, and thus not an employee under Workmen's Compensation law).

⁷ *Cox v. Hickman*, 8 H.L.C. 268, 11 Eng. Rep. 431 (1860).

⁸ *Cothran v. Marmaduke & Brown*, 60 Tex. 370 (1883) (holding that one who is to receive a share of the profits of the business as consideration for a loan is a partner); *Steger v. Greer*, 228 S.W. 304 (Tex. Civ. App. 1921) error *dism.*; *Avery v. Llano Cotton Seed Oil Mill Ass'n*, 196 S.W. 351 (Tex. Civ. App. 1917) error *ref.*; *Fink v. Brown*, 183 S.W. 46 (Tex. Civ. App. 1916), *rev'd* as to alleged partner, 215 S.W. 846 (Tex. Comm. App. 1919); *Fouke v. Brengle*, 51 S.W. 519 (Tex. Civ. App. 1899); *Dilley v. Abright*, 48 S.W. 548 (Tex. Civ. App. 1898). It has been said, however, that the English net profits rule has never been adopted in Texas, although the language of some of the early cases led to some confusion. *Gardner v. Wesner*, 55 S.W.2d 1104, 1106 (Tex. Civ. App. 1932) error *ref.*

the business, thus making it unfair to hold him accountable for the obligations of the business. The Texas courts, like those of most jurisdictions, eventually recognized this defect, and they have clearly rejected participation in profits as an arbitrary test of the existence of a partnership;⁹ however, they have not found it so easy to develop a definitive test of partnership. In fact, some courts have said that it is impossible to formulate such a definition or test.¹⁰ On the other hand, after dealing with a great many cases involving the question of the existence of a partnership, the Texas courts seem to have developed an approach to the problem that works out fairly well in most cases. They have taken the position, adopted by most courts, that while participation in profits is "presumptive" evidence of the existence of a partnership, it is not conclusive and can be overcome by a showing of the absence of other partnership attributes.¹¹ Moreover, they have succeeded in formulating a general test which at least serves as a starting point for the determination of whether the relation exists, as follows: "a community of interests, the common enterprise, its operation for the joint account, and a right in each owner to share as a principal in its profits as such."¹² While this formulation does not furnish the courts with a precise and completely objective yardstick, since several of the terms are elastic and need definition themselves, it does establish the general principle that the alleged partner's interest in the business and in the profits must be that of an owner.¹³

⁹ *Fink v. Brown*, 215 S.W. 846 (Tex. Comm. App. 1919), reversing 183 S.W. 46 (Tex. Civ. App. 1916) as to liability of alleged partner; *Gardner v. Wesner*, 55 S.W.2d 1104 (Tex. Civ. App. 1932) error ref. The Texas courts have recognized that profit sharing may be used by businesses in non-partnership arrangements; and there are decisions holding that there was no partnership where a share of the profits was used as a measure of rent, *Fink v. Brown*, supra; interest, *Eddingston v. Acom*, 259 S.W. 948 (Tex. Civ. App. 1924) error dism.; compensation for services, *Goode v. McCartney*, 10 Tex. 193 (1853); commission for agent or broker, *Buzard v. Bank*, 67 Tex. 83, 2 S.W. 54 (1886).

¹⁰ *Moore v. Scott*, 16 S.W.2d 1100, 1106-07 (Tex. Civ. App. 1929) error dism.; *Millers' Indemnity Underwriters v. Patten*, 238 S.W. 240, 242 (Tex. Civ. App. 1922), aff'd, 250 S.W. 154 (Tex. Comm. App. 1923).

¹¹ *Fink v. Brown*, 215 S.W. 846 (Tex. Comm. App. 1919); *Eddingston v. Acom*, 259 S.W. 948 (Tex. Civ. App. 1924) error dism.; *Southern Surety Co. v. Texas Employers' Ins. Ass'n*, 2 S.W.2d 310 (Tex. Civ. App. 1927) error ref.; see also *Davis v. Gilmore*, 244 S.W.2d 671 (Tex. Civ. App. 1951) error ref.

¹² This test seems to have been first formulated by the Texas Supreme Court in *Freeman v. Huttig Sash & Door Co.*, 105 Tex. 560, 153 S.W. 122 (1913). It has been frequently cited by the courts as the test of the existence of a partnership in Texas. See, e.g., *Fink v. Brown*, 215 S.W. 846, 849 (Tex. Comm. App. 1919); *Ogus, Rabinovich & Ogus v. Foley Bros. Dry Goods Co.*, 252 S.W. 1048, 1051 (Tex. Comm. App. 1923); *Gardner v. Wesner*, 55 S.W.2d 1104, 1106 (Tex. Civ. App. 1932) error ref.

¹³ See *Strawn Nat'l Bank v. Marchbanks*, 74 S.W.2d 447, 449 (Tex. Civ. App. 1934) error ref., in which it is stated that the Texas courts have given meaning to the phrase "interest in profits as profits," criticized by some writers as meaningless, to the effect that the profit sharer is a partner only if his interest in the profits is that of a part owner.

The act's definition of a partnership, "an association of two or more persons to carry on as co-owners a business for profit,"¹⁴ does not do away with this uncertainty, since reasonable men may differ as to whether the facts of a particular case establish co-ownership. In fact, the final draftsman of the act conceded that it is impossible for any statutory statement of the law to eliminate the uncertainties inherent in the question of whether or not a particular association is a partnership, which, unlike other kinds of business associations, is not formed by the happening of an event or the compliance with certain formal requirements specified in a statute as necessary to its formation.¹⁵ Section 7 of the act does afford some help by laying down a series of rules to assist in the determination of whether a partnership exists, including the principle now accepted in Texas that profit sharing is *prima facie* evidence that the profit sharer is a partner in the business but that no such inference shall be drawn if the profits are received in payment of such things as a debt, wages, or interest. "In spite of these rules, however, it will always be possible to give a number of real or supposititious cases in which men will differ as to whether the facts show co-ownership of a given business."¹⁶

On the other hand, in at least one respect the act may reduce the existence-of-a-partnership uncertainty, and that is in emphasizing that "co-ownership" as used in section 6 involves "the power of ultimate control" over the business.¹⁷ While the Texas courts

¹⁴ § 6.

¹⁵ See Lewis, *The Uniform Partnership Act*, 24 *Yale L.J.* 617 (1915), where the author states at 622:

On the other hand, an infinite number of combinations may result in co-ownership of a business. Partnership is the residuum, including all forms of co-ownership, of a business except those business associations organized under a specific statute.

If a partnership act were to declare that a partnership was not formed until the formal requirements of the statute were complied with, it would not be a statute regulating common law partnerships, but one abolishing common law partnership and establishing a new form of statutory association. If no formal act can be specifically designated as a necessary prerequisite to the formation of a common law partnership, it follows that it is not always easy to determine whether the acts proved indicate co-ownership of a business. Ownership, whether the ownership of a business or the separate ownership of personal or real property, involves the idea of control; but the degree of control necessary is incapable of exact definition. Neither is it possible to catalogue all the possible combinations of fact, which, when found to exist, will conclusively prove ownership.

As to the difficulty of defining a partnership, see Crane, *Partnership* § 5 (2d ed. 1952); Mechem, *Partnership* § 1 (2d ed. 1920); Lindley, *Partnership* 1-5 (2d Am. ed. 1888) (quoting numerous definitions).

¹⁶ Lewis, *supra* note 15, at 622.

¹⁷ Commissioners' Note to § 6; see also statement of Professor Lewis quoted in note 15 *supra*.

Of course, the fact that the parties agree that the management of the everyday affairs of the business shall be concentrated in less than all of the parties does not automatically mean there can be no partnership, Crane, *Partnership* § 14 (2d ed. 1952), since the "power

have sometimes stressed the factor of control over the business as evidence of the existence of a partnership,¹⁸ in other cases they have ignored this factor which, if taken into account, may very well have produced a different result.¹⁹

Moreover, adoption of the act would eliminate the vague "partners as to third persons" doctrine that has found some support in the Texas cases. Under this doctrine the courts apply a less strict test and require less evidence to establish a partnership as to a third person, even in the absence of the elements of partnership by estoppel, than to show the existence of a partnership as among the partners.²⁰ In Texas the doctrine manifests itself in a tendency on the part of the courts to give more weight to the "actual intention," including expressions of intent, of the alleged partners when the question involves rights and obligations among themselves,²¹ than they do when the dispute is between the alleged partner and a third person.²² One objection to the doctrine is its

of ultimate control" presumably refers to the right of each partner to have a voice in basic changes in policy that will affect the fundamental basis and purpose of the business.

In spite of the fact that the Commissioners' Note to § 6 makes it very clear that "co-ownership" as used in § 6 does not mean co-ownership of the property or capital employed in the business, some courts in states which have adopted the act have said that co-ownership of the partnership property is necessary to the existence of a partnership. *Walker, Mosby & Calvert, Inc. v. Burgess*, 153 Va. 779, 151 S.E. 165 (1930); see also *Nelson v. Abraham*, 29 Cal. 2d 745, 749, 177 P.2d 931, 933 (1947); *Northampton Brewery Corp. v. Lande*, 138 Pa. Super. 235, 239, 10 A.2d 583, 585 (1940). On the other hand, other courts have recognized that it is co-ownership of the business, and not of the partnership property, that is the prerequisite. *Tower v. Sobelman*, 86 F. Supp. 369 (E.D. Pa. 1949); *Provident Trust Co. v. Rankin*, 333 Pa. 412, 5 A.2d 214 (1939).

¹⁸ *Davis v. Gilmore*, 244 S.W.2d 671 (Tex. Civ. App. 1951) error ref.

¹⁹ See, e.g., *Strawn Nat'l Bank v. Marchbanks*, 74 S.W.2d 447 (Tex. Civ. App. 1934) error ref. (X proposed to furnish the grass and care for cattle to be purchased in Y's name with money put up by Y, the profits on the sale of the cattle to be split equally. Held, X was not Y's partner in the venture, the court emphasizing X's lack of a property interest in the cattle.)

²⁰ See *Harding v. Giddings*, 256 S.W. 305, 307 (Tex. Civ. App. 1923), rev'd, 267 S.W. 976 (Tex. Comm. App. 1925); *Altgelt v. Elmendorf*, 86 S.W. 41, 43 (Tex. Civ. App. 1905) motion for rehearing granted, for statements indicating that the Texas Supreme Court applies different tests in the two types of cases.

²¹ *Donald v. Phillips*, 13 S.W.2d 74 (Tex. Comm. App. 1929) and cases cited note 22 supra. But see Commission of Appeals' decision in *Harding v. Giddings*, supra note 20 (the Court of Civil Appeals held no partnership because terms of agreement denominated a "lease contract" did not evidence an intention on the part of the parties to become partners. The Commission of Appeals reversed, saying: "The terms of this contract evidence an intention on the part of the parties thereto to engage in a business undertaking with each other, which in law constitutes a partnership." 267 S.W. 976, 977.)

²² "The question of the intention of the parties is proper for a jury to take into consideration in determining whether or not a partnership has been actually formed. It is not, however, absolutely necessary for the jury to find that each party actually intended a partnership to be formed in order to create said relationship. Regardless of the intention of the parties, if, as a matter of fact, a partnership was actually formed, all partners thereby became bound as such." *Allison v. Campbell*, 35 S.W.2d 776, 778 (Tex. Civ. App. 1931) error dism. For other statements to the effect that as to third persons parties may be partners in spite of their intention that there should be no partnership, see *Freeman v. Huttig Sash & Door Co.*, 105 Tex. 560, 571-72, 153 S.W. 122, 125 (1913); *Brown v. Watson*,

vagueness and uncertainty.²³ In addition there is no valid reason for imposing liability to a third person on someone associated with the owner of a business in some such capacity as lender or landlord, where there are no elements of estoppel present, if there are missing from their relationship certain attributes essential to their being held partners *inter se*. The act eliminates these objections by declaring that except in the case of partnership by estoppel "persons who are not partners as to each other are not partners as to third persons."²⁴

In connection with the related problem of partnership by estoppel, the act also eliminates an uncertainty that exists in the present Texas law. Under the doctrine of "partner by estoppel" one (called the "ostensible partner") who has held himself out, or permitted himself to be held out as a partner of another, is estopped to deny the existence of a partnership as against one who has extended credit to the supposed partnership in reliance on such holding out.²⁵ There is a split of authority among the states as to whether mere inaction on the part of a person who, to his knowledge but without his permission or assent, is being held out as a partner by another is sufficient to make the former a partner by estoppel.²⁶ This exact question seems never to have been decided in Texas, although there is language in at least one case indicating that the doctrine may be applied where the ostensible partner was merely aware of the holding out and did nothing about it.²⁷ The Commissioners decided that those authorities requiring actual consent represent "the better reasoning,"²⁸ and they followed them in section 16(1).²⁹

72 Tex. 216, 221, 10 S.W. 395, 396 (1888); *Cochran v. Marmaduke & Brown*, 60 Tex. 370, 372 (1883).

²³ Confusing statements such as the following are not uncommon: "And while profit-sharing may, in a controversy between third parties, on the one hand, and the supposed partners, on the other, be evidence . . . of partnership, it is so (to the extent it is true) because in that situation actual intention may be made to yield to 'legal intentions' . . . whereas in charges and countercharges *inter sese* actual intent should control." *Donald v. Phillips*, 13 S.W.2d 74, 77 (Tex. Comm. App. 1929). "What they call their agreement and make it determine their relation unless their actual intent is nevertheless to be partners." 32 Tex. Jur., Partnership § 13 (1934) (referring to the rights of the parties as among themselves).

²⁴ § 7(1).

²⁵ Representation by ostensible partner: *Walker v. Brown*, 66 Tex 556, 1 S.W. 797 (1886); *Crozier, Rhea & Co. v. Kirker*, 4 Tex. 252 (1849). Holding out by another: *Bivins v. Oldham*, 224 S.W. 240 (Tex. Civ. App. 1920) error ref.; *Southern Agricultural Works v. Sims*, 26 S.W. 614 (Tex. Civ. App. 1894).

²⁶ See Commissioners' Note to § 16; *Crane, Partnership* § 36 (2d ed. 1952).

²⁷ "It would appear that a reasonably prudent man, knowing that his name was improperly used in a business, would have notified all persons whom he knew or had reason to think were relying on the existence of such partnership." *Bivins v. Oldham*, 224 S.W. 240, 244 (Tex. Civ. App. 1920) error ref.

²⁸ Commissioners' Note to § 16; *Lewis*, *supra* note 15, at 625.

²⁹ Note, however, that even following the adoption of the act in Maryland, it has been

The position taken by the act on this point is in line with usual estoppel principles, under which a party is estopped to deny a fact only if he creates or contributes to misleading appearances or acquiesces in their creation by another; and it is supported by the argument that it is unfair to require one whose name is being used without permission to take affirmative action to dispel the misleading appearances thereby created.

II. PROBLEMS INVOLVING PARTNERSHIP PROPERTY

Partnership property and the interest of the partners, their assignees and creditors therein, is one area of partnership law which has given rise to a great many problems, and in which the act makes some of its most significant contributions. The main source of difficulty is that the early common-law courts, recognizing that partners understand themselves to be co-owners of the business, felt constrained to apply one of the usual common-law forms of co-ownership to partnership property. Thus they decided that partners hold partnership property as joint tenants,³⁰ and they applied the various legal incidents of such tenancy, although frequently inappropriate to property devoted to a business enterprise. The act, on the other hand, proceeds upon the theory that the orthodox forms of common-law co-ownership do not fit the partnership relation, and it creates an entirely new form of co-ownership, the incidents of which are designed to meet the practical necessities of the relationship.³¹

stated that knowledge by the ostensible partner of the unauthorized holding out is sufficient to make him a partner by estoppel unless he does all that a reasonable and honest man would do to deny the relationship. *McBriety v. Phillips*, 180 Md. 569, 578, 26 A.2d 400, 405 (1942). But see Note, 6 Md. L. Rev. 337 (1942), which suggests that the court in the *McBriety* case may merely be saying that under some circumstances failure to repudiate the holding out may be evidence of the ostensible partner's consent.

³⁰ *Heydon v. Heydon*, 1 Salk. 392, 91 Eng. Rep. 340 (K.B. 1693), explained in *Lewis*, supra note 15, at 630-31.

³¹ Many partnership property problems could also have been solved by defining the partnership as a separate legal person or entity which owns the property devoted to the business. This entity theory of the nature of a partnership is sometimes called the "mercantile theory" by its proponents on the ground that businessmen think of partnerships as separate persons. It is contrary to the common-law idea that the legal nature of a partnership is an association of persons carrying on a business as co-owners, or the so-called "aggregate" theory. See *Crane, Partnership* § 3 (2d ed. 1952). The Texas courts, following the common-law view, have repeatedly stated that the partnership is not a separate legal entity, a pronouncement that has sometimes affected the outcome of the problem at hand. *Frank v. Tatum*, 87 Tex. 204, 25 S.W. 409 (1894) (since partnership not a legal entity, all partners must be joined as parties defendant, and dismissal as to any deprives court of jurisdiction over the partnership property); *Aboussie v. Aboussie*, 270 S.W.2d 636 (Tex. Civ. App. 1954) error ref. (since partnership not a legal entity, minor child barred from suing partners among whom was her father); *Feldman v. Seay*, 291 S.W. 350 (Tex. Civ. App. 1927) (since partnership not a legal entity, partnership cannot be sued in firm name

A. *What is Partnership Property?*

Before the various problems involving partnership property under Texas law are developed, the preliminary, and often difficult, question of what is partnership property should be mentioned. Property originally belonging to a partner, or purchased with money furnished by him, which is used for partnership purposes may be separate property of the partner, the use of which is contributed to the partnership, or it may be that partner's contribution to the capital of the partnership and thus become partnership property. Likewise, property purchased with partnership funds may be partnership property, or property owned by the partners as co-tenants, or even property of one of the partners, the purchase price being a withdrawal from the partnership by him.³² Whether a specific asset is separate or partnership property depends upon the intention and understanding of the partners, under Texas law³³ and apparently under the act.³⁴ Unfortunately it is frequently very difficult to discover the intention of the partners, and resolution of the question may be largely a matter of speculation.³⁵ The act furnishes some help by providing that property acquired with partnership funds is partnership property unless a contrary intention appears,³⁶ and the same appears to be true under Texas law.³⁷

and all partners must be joined as parties defendant; later changed by rule of court, see *infra*). On the other hand, the partnership has been given separate identity for certain limited purposes by statute or rule of court. See, e.g., Tex. Rev. Civ. Stat. art. 2033 (1925) (judgment binding partnership property may be had by service of citation upon one partner); Tex. R. Civ. P. 28 (1941) (partnership may be sued in the firm name).

Dean Ames, the original draftsman of the act, was an advocate of the entity theory and defined the partnership as a legal person in the first two drafts. See Lewis, *supra* note 15, at 640. Dean Lewis, who upon Ames' death became the draftsman, opposed the entity theory on the ground that while it solves some difficulties, it creates others; and, with the approval of the Commissioners, he did not draft the act on that theory. *Ibid.* The act has been vigorously criticized by Professor Crane for its failure to define the partnership as a legal person and staunchly defended by Dean Lewis in a spirited exchange of articles. Crane, *The Uniform Partnership Act—A Criticism*, 28 Harv. L. Rev. 762 (1915); Lewis, *The Uniform Partnership Act—A Reply to Mr. Crane's Criticism*, 29 Harv. L. Rev. 158, 291 (1916); Crane, *The Uniform Partnership Act and Legal Persons*, 29 Harv. L. Rev. 838 (1916).

³² The distinction between separate and partnership property is important in determining the rights of partners and creditors in the property.

³³ *Logan v. Logan*, 138 Tex. 40, 156 S.W.2d 507 (1942); *Bivins v. Proctor*, 80 S.W.2d 307 (Tex. Comm. App. 1935); *Masterson v. Allen*, 69 S.W.2d 539 (Tex. Civ. App. 1934) error ref.; *Williams v. Meyer*, 64 S.W. 66 (Tex. Civ. App. 1901) error ref.; *Luck v. Hopkins*, 54 S.W. 429 (Tex. Civ. App. 1899) error ref.

³⁴ Such seems to be the effect of the words "on account of the partnership" in § 8(1) of the act.

³⁵ See, e.g., *Luck v. Hopkins*, 54 S.W. 429 (Tex. Civ. App. 1899) error ref.

³⁶ § 8(2).

³⁷ See *Snaman v. Lane*, 184 S.W. 366, 367 (Tex. Civ. App. 1916) error ref.; *Luck v. Hopkins*, 54 S.W. 429, 430 (Tex. Civ. App. 1899) error ref.

B. *Rights of the Partners in Partnership Property*

The Texas courts, like other common-law courts,³⁸ have long recognized that it is impossible to apply to property devoted to a business enterprise all of the incidents of joint tenancy, under which, for example, any of the partners would be free to do as he wished with his interest in the common property, irrespective of the claims of the other partners arising out of the business. Therefore, although co-ownership of partnership property is an outgrowth of common-law joint tenancy, certain distinct characteristics of partnership tenure have been developed.

The courts have adapted common-law co-ownership to partnership property by holding that each partner has an equitable interest in or lien on the entire partnership property to the extent necessary to carry out the partnership purposes.³⁹ Under this principle, sometimes called the doctrine of "partners' equities,"⁴⁰ each partner is entitled to have the partnership property applied to the payment of partnership debts.⁴¹ Thus, a partner may not without the consent of his co-partners assign or mortgage his share of part or all of the partnership property, free of his co-partners' liens, leaving them to satisfy partnership debts out of their shares.⁴² Likewise, although in Texas a partner may fasten a homestead exemption on his share of partnership real property,⁴³ he may not do so without the consent of his co-partners if the partnership is insolvent.⁴⁴ The equitable lien of each partner on all the partnership property not only pro-

³⁸ For example, at an early date it was held in England that the survivorship incident of joint tenancy does not apply to the beneficial title in the case of partnership joint tenancy. *Martin v. Crump*, 2 Salk. 444, 91 Eng. Rep. 385 (K.B. 1698).

³⁹ "As every partner is liable for the debts of his firm, and owns its property in common with other partners, it is his right to have the common property applied to the payment of partnership debts, and all the other partners, without his consent, cannot take this right from him. This right is sometimes said to give every partner an equitable lien on firm assets. . . ." *Wiggins v. Blackshear*, 86 Tex. 665, 668-69, 26 S.W. 939, 940 (1894).

⁴⁰ *Crane, Partnership* § 40 (2d ed. 1952).

⁴¹ *Warren v. Wallis, Landes & Co.*, 38 Tex. 225 (1873); *Egan v. American State Bank*, 67 S.W.2d 1081 (Tex. Civ. App. 1934) error ref.; *Bolding v. Bolding*, 200 S.W. 587 (Tex. Civ. App. 1918) error dism.

⁴² *Oliphant v. Markham*, 79 Tex. 543, 15 S.W. 569 (1891) (pledge to secure separate indebtedness); *Sherk v. First Nat'l Bank*, 206 S.W. 507 (Tex. Comm. App. 1918) (mortgage to secure separate indebtedness); *Kennard v. Kennard*, 84 S.W.2d 315 (Tex. Civ. App. 1935) error dism. (assignments to secure separate indebtedness).

Likewise, a separate creditor of one of the partners may not attach his interest in partnership property, free of the equitable liens of the other partners. *Warren v. Wallis, Landes & Co.*, supra note 41.

⁴³ *Egan v. American State Bank*, 67 S.W.2d 1081 (Tex. Civ. App. 1934) error ref.

⁴⁴ *Egan v. American State Bank*, supra note 43; *Williams v. Meyer*, 64 S.W. 66 (Tex. Civ. App. 1901). It has been held, however, that if the firm is solvent, a partner can subject his interest in partnership realty to a homestead exemption without his co-partners' consent, and that his interest in such property cannot be charged with future partnership debts even if the firm later becomes insolvent. *Swearingen v. Bassett*, 65 Tex. 275 (1886).

protects him against having to bear a disproportionate amount of the partnership debts upon dissolution, but it also prevents firm assets from being removed before the accounts are settled among the partners and secures to each his proper share of the assets upon dissolution.⁴⁵ In order that the surviving partners may receive the same protection upon the death of a partner, the Texas cases hold that if it is necessary for partnership real property to be used to pay partnership debts or settle partnership accounts, the surviving partners take the full equitable title for such purpose, instead of taking as tenants in common with the heirs of the deceased partners.⁴⁶ Still another aspect of the partners' equities doctrine is that it secures each partner in his right to have the partnership property remain in the business for the proper conduct of firm affairs so long as the partnership continues. This right, together with the principle that partnership property belongs to the firm and the partners have no individual property right in, and no right during the existence of the partnership to exclusive possession or use of, any partnership property,⁴⁷ insure that such property is available for firm business during the existence of the partnership.

Out of the partners' equities doctrine has arisen the principle that a partner's interest in partnership property is merely his proportionate share of the surplus remaining after the payment of partnership debts and the settlement of accounts among the partners.⁴⁸ Such interest is all that he may effectively assign or mortgage without the consent of his co-partners,⁴⁹ for he has no specific in-

⁴⁵ *Harrison v. Bailey*, 260 S.W.2d 702 (Tex. Civ. App. 1953). See *Wiggins v. Blackshear*, 86 Tex. 665, 669, 26 S.W. 939, 940 (1894).

⁴⁶ *Martin v. Dial*, 57 S.W.2d 75 (Tex. Comm. App. 1933). See *Miller v. Howell*, 234 S.W.2d 925, 930 (Tex. Civ. App. 1951); *Donnell v. Talley*, 104 S.W.2d 920, 924 (Tex. Civ. App. 1937) error dism. by agr.

The surviving partners may sell the partnership realty to pay firm debts or settle partnership accounts. *Smith v. Wayman*, 148 Tex. 318, 224 S.W.2d 211 (1949). See *Dial v. Martin*, 37 S.W.2d 166, 178 (Tex. Civ. App. 1931), rev'd on other grounds, 57 S.W.2d 75 (Tex. Comm. App. 1933). Although the surviving partners can only convey equitable title, the purchaser can compel the heirs of the deceased partner to convey legal title to him. See *Smith v. Wayman*, 216 S.W.2d 837, 840 (Tex. Civ. App. 1948), aff'd, 148 Tex. 318, 224 S.W.2d 211 (1949); *Dial v. Martin*, supra at 178.

If partnership realty is not needed to pay firm debts or to adjust the accounts among the partners, the surviving partners become tenants in common with the heirs of the deceased partner. *Donnell v. Talley*, supra; *Isbell v. Southworth*, 114 S.W. 689 (Tex. Civ. App. 1908).

⁴⁷ *Warren v. Wallis, Landes & Co.*, 38 Tex. 225 (1873). See *Sherk v. First Nat'l Bank*, 206 S.W. 507, 509 (Tex. Comm. App. 1918); *Miller v. Howell*, 234 S.W.2d 925, 930 (Tex. Civ. App. 1951); *Egan v. American State Bank*, 67 S.W.2d 1081, 1084 (Tex. Civ. App. 1934) error ref.

⁴⁸ *Oliphant v. Markham*, 79 Tex. 543, 15 S.W. 569 (1891); *Sherk v. First Nat'l Bank*, supra note 47; *Egan v. American State Bank*, supra note 47. See *Miller v. Howell*, 234 S.W.2d 925, 930 (Tex. Civ. App. 1951).

⁴⁹ *Oliphant v. Markham*, supra note 48; *Still v. Focke*, 66 Tex. 715, 2 S.W. 59 (1886); *Sherk v. First Nat'l Bank*, supra note 48. For the effect of a conveyance of specific part-

terest in any particular part of the firm property.⁵⁰ Unfortunately, there is some confusion in the Texas cases as to the effect of a purported conveyance of specific partnership property by one partner without his co-partners' consent at a time when the partnership is solvent.⁵¹ One case seems to hold that such a conveyance passes nothing because the partner's interest in the specific property is too remote to permit him to convey any interest therein.⁵² Other cases, however, indicate that if the partnership is solvent, a mortgage or other conveyance of specific partnership property gives the mortgagee or grantee a lien on the property to the extent of the conveying partner's interest in the surplus,⁵³ or even an undivided one-half interest in the property conveyed.⁵⁴

There are other problems in connection with the interest of the partners in partnership property which are not eliminated by the partners' equities doctrine. For example, the Texas courts hold that if a partner assigns his interest in all of the partnership property, either to a third person or to a co-partner, the partnership is dissolved.⁵⁵ Frequently such an assignment to a third person is made simply to secure an indebtedness of the assigning partner, who does not intend to disassociate himself from the business.⁵⁶ Under such circumstances there seems to be no reason why the assignment should necessarily result in dissolution. Moreover, even where the assigning partner does intend to terminate his association with the partnership, there is no reason why, in the case of a partnership for a term, the remaining partners should be prevented from carrying on the business in accordance with the partnership agreement and should be forced to wind up the partnership and divide the property.⁵⁷ Thus in the case of an assignment for se-

nership property made with the consent of the other partners, see text accompanying notes 68-74 *infra*.

⁵⁰ See cases cited note 47 *supra*.

⁵¹ Of course, if the partnership is insolvent, such a conveyance passes nothing, since there is no surplus in which the conveying partner is entitled to share. *Sherk v. First Nat'l Bank*, 206 S.W. 507 (Tex. Comm. App. 1918).

⁵² *Oliphant v. Markham*, 79 Tex. 543, 15 S.W. 569 (1891).

⁵³ See *Sherk v. First Nat'l Bank*, 206 S.W. 507, 509 (Tex. Comm. App. 1918).

⁵⁴ *Tom v. First Nat'l Bank*, 104 S.W.2d 130 (Tex. Civ. App. 1937) error dism.

⁵⁵ *Moore v. Steele*, 67 Tex. 435, 3 S.W. 448 (1887) (transfer to third person); *Sherk v. First Nat'l Bank*, 206 S.W. 507 (Tex. Comm. App. 1918) (transfer to co-partner).

⁵⁶ See *Lewis*, *The Uniform Partnership Act*, 24 Yale L.J. 617, 626 (1915).

⁵⁷ Of course, it is clear that the assignee cannot be permitted to step into his assignor's shoes as a partner without the consent of the non-assigning partners. The right of partners to select their co-partners is based upon the facts that partners stand in a fiduciary relation to each other and that each has the power to dispose of firm property and to incur obligations binding upon his co-partners. This idea is commonly expressed by the statement that an important element of the partnership relation is *delectus personae*, the choice of the person. See *Johnston v. Winn*, 105 S.W.2d 398, 400 (Tex. Civ. App. 1937).

curity the Texas courts have not solved the problem of how to protect the assignee of a partner's interest without unduly disturbing his relationship with the business and the rights of the remaining partners.

Section 25(1) of the act attacks these problems caused by applying an orthodox common-law form of co-ownership to partnership property by establishing a new form of co-ownership of property for partnerships, called "tenancy in partnership." Although the act does not define the partnership as a separate legal person,⁵⁸ the incidents of tenancy in partnership enumerated in section 25(2) are consistent with the entity theory.⁵⁹ The incidents incorporate all of the desirable features of the partners' equities doctrine as applied in Texas and eliminate some of the problems that still exist in the Texas law.

The first incident of tenancy in partnership is that each partner has the right to possess firm property for partnership purposes, but no right to possess it for any other purpose, which is also the rule under the Texas cases.⁶⁰ In section 25(2)(b) it is provided that a partner's right in specific partnership property is not assignable except in connection with the assignment of rights of all the partners in the same property.⁶¹ All that a partner may separately assign under the act is his interest in the partnership, which is defined in section 26 as "his share of the profits and surplus." Thus, under the act, as under the partners' equities doctrine, a partner is not free to remove specific property from the partnership without the consent of his co-partners. Tenancy in partnership also gives some measure of protection against the removal of partnership property from the reach of partnership creditors, section 26(2)(c) providing that when partnership property is attached for a partnership debt, no right under the homestead or exemption laws can be claimed by the partners.⁶² A fourth incident of tenancy in partnership is that a deceased partner's right in specific partnership property vests, for partnership purposes, in the surviving partner which, in effect, is also the rule under present Texas law.⁶³ The final incident is that a partner's right in specific partnership pro-

⁵⁸ See note 31 *supra* for discussion.

⁵⁹ Crane, *Partnership* § 40 (2d ed. 1952); Crane, *The Uniform Partnership Act—A Criticism*, 28 *Harv. L. Rev.* 762, 772-73 (1915). Section 25(2) lists the incidents.

⁶⁰ See note 47 *supra* and accompanying text.

⁶¹ Section 25(2)(b) also deals with the rights of separate creditors in specific partnership property. See notes 101-04 *infra* and accompanying text.

⁶² For a comparison between § 25(2)(c) and the present Texas law, see notes 82-86 *infra* and accompanying text.

⁶³ See note 43 *supra* and accompanying text; note 46 *supra*.

perty is not subject to dower, curtesy, or allowance to widows, heirs, or next of kin.

The act's treatment of the property rights of a partner decidedly improves upon the Texas law of common-law co-ownership as modified by the partners' equities principle. In the first place the act is realistic in abandoning traditional common-law co-ownership as unsuited to the ownership of property devoted to a business enterprise. In establishing a new kind of co-ownership for the special situation of the partnership, it eliminates the necessity of modifying an inappropriate form of ownership by exceptions, which is always an unsatisfactory way of dealing with an unique problem.

More important, however, is the manner in which the act deals with some of the specific problems not solved by the partners' equities doctrine. The provision of section 25(2)(b) that a partner's right in specific partnership property can only be assigned in connection with an assignment by all the partners of their rights therein clears up the confusion as to what interest passes when one partner attempts a separate assignment. Under this provision such an assignment is invalid and no interest in the property passes to the assignee.⁶⁴ Even under the act, however, an attempted assignment by a partner of his rights in all the partnership property may be regarded as a valid assignment of his interest in the partnership.⁶⁵

In section 27 it is provided that an assignment of a partner's interest in the partnership does not necessarily dissolve the partnership, nor does it give the assignee the right to take his assignor's place as an active partner, but it merely gives him the right to receive the profits to which his assignor is entitled under the partnership agreement.⁶⁶ Thus, the act, unlike the Texas cases, solves completely the problem of how to protect the assignee of a part-

⁶⁴ Johnston v. Ellis, 49 Idaho 1, 285 Pac. 1015 (1930); Windom Nat'l Bank v. Klein, 191 Minn. 447, 254 N.W. 602 (1934); Lewis, *supra* note 56, at 634 ("... a partner may assign partnership property for a partnership purpose, but if he attempts to assign the property for his own purposes he makes no assignment at all, because the Act destroys the quality of assignability for any but a partnership purpose.") According to the Commissioners' Note to § 25, an attempted assignment by a partner of his interest in specific partnership property cannot be treated as a conveyance of a fractional part of his interest in the partnership because of the impossibility of determining what fractional part of his interest he intended to assign.

⁶⁵ Johnston v. Ellis, note 64 *supra*; Commissioners' Note to § 25.

⁶⁶ Section 27 is designed to protect the rights of the non-assigning partners from disturbance only during the balance of the term of the partnership remaining after the assignment. Under § 32(2) the purchaser of a partner's interest may obtain a dissolution of the partnership by decree of court after the specified term of the partnership has expired, or at any time if the partnership was a partnership at will at the time of the assignment.

ner's interest without unduly disturbing the rights of the remaining partners, and of how to protect the relationship with the business of the assigning partner where he has merely assigned his interest to secure a separate debt.

Section 25(2)(d), which provides that the title to the specific partnership property passes to the surviving partners upon the death of a partner, also is an improvement over the present Texas law. Although the Texas cases hold that the surviving partners take equitable title to partnership real estate if it is needed to pay partnership debts or settle partnership accounts, and that they may sell the property for those purposes, the purchaser only acquires equitable title and must seek court aid to compel the heirs of the deceased partner to convey the legal title to him.⁶⁷ Under section 25(2)(d), on the other hand, the surviving partners may under such circumstances convey full legal title to partnership real estate without any joinder in the conveyance by the heirs or any aid from the courts.

C. Rights of Partnership Creditors in Partnership Property

One of the most serious defects in the present Texas law of partnerships is its failure to afford adequate protection to the rights of partnership creditors. Under Texas law partnership creditors have no lien or claim on partnership assets until acquired by attachment or execution.⁶⁸ Their only right in partnership property is one of subrogation to the partners' right to have firm assets applied to the payments of firm debts in order to do justice among the partners.⁶⁹ This right is sometimes called a quasi-lien.⁷⁰ Since

⁶⁷ See note 46 *supra*.

⁶⁸ *Wiggins v. Blackshear*, 86 Tex. 665, 26 S.W. 939 (1894); *Stansell v. Fleming*, 81 Tex. 294, 16 S.W. 1033 (1891); *White v. Parish*, 20 Tex. 689 (1858); *Hawkins v. Western Nat'l Bank*, 146 S.W. 1191 (Tex. Civ. App. 1912); *Waples-Platter Co. v. Mitchell*, 35 S.W. 200 (Tex. Civ. App. 1895) error ref.; *Johnston v. Standard Shoe Co.*, 24 S.W. 580 (Tex. Civ. App. 1893).

⁶⁹ The following language is found in *Wiggins v. Blackshear*, 86 Tex. 665, 669, 26 S.W. 939, 940 (1894):

That a partnership creditor has no specific lien, either legal or equitable, upon partnership assets, any more than any individual creditor has upon the estate of his debtor, is so firmly established that citation of authority in support of the proposition is useless; but they may acquire liens by contract, or through the process of a court by which the creditors may acquire liens on specific property.

The rule is thus well stated: "A creditor of a partnership has, as a general rule, no direct lien upon the partnership property until he acquires it by legal process, that is, by the levy of an attachment or of an execution. His indirect or quasi lien is derived from the lien or equity of the individual partners. If the partners are not in a condition to enforce an equitable lien upon the partnership property, the creditors of the partnership cannot enforce a lien derived from them or from one of them. The equity of the partnership creditor continues so long as the equity of the individual partner continues, and no longer." *Jones, Liens*, 788.

When, however, the property of a partnership passes into the custody of a court for

a general creditor's quasi-lien is a derivative interest, dependent upon the equitable liens of the partners, it is lost when the partners lose their liens. Thus, in the following situations the equities of the partners in specific partnership property, and with them the quasi-liens of partnership creditors, are extinguished, thereby reducing the amount of property to which such creditors have first claim: (a) partnership property is applied to the payment of the separate debts of one or more of the partners with the consent of the others;⁷¹ (b) a partner fastens a homestead exemption on his interest in firm property with the consent of his co-partners;⁷² (c) partnership assets are transferred to some of the partnership creditors in payment of their claims; (d) partnership property is transferred to one or more of the partners with the consent of the others; (e) all the partnership assets are divided among the partners.⁷³ Likewise, if one of two partners sells his interest in the partnership, or in all its property, to his co-partner without reserving his equitable right to have the partnership property applied to the payment of firm debts, the partnership is dissolved, its property becomes the separate property of the purchasing partner and the equitable lien of the selling partner, and the rights of the firm creditors through him, are lost.⁷⁴

In the latter three situations, of course, the property is added to the separate property of one or more of the partners, where the creditors of the partnership may still reach it. It might therefore appear that the partnership creditors are not injured by such transfers of the partnership property, even if the partnership is in-

administration, as in cases of bankruptcy or assignment made by an insolvent firm, then the court will administer it as was the right of the several partners to have it administered while controlled by themselves.

In such cases the court's action is based as fully upon the rights of the partners as between themselves as upon the rights of creditors. . . .

⁷⁰ *Wiggins v. Blackshear*, supra note 69; *Hawkins v. Western Nat'l Bank*, 146 S.W. 1191 (Tex. Civ. App. 1912); *Johnston v. Standard Shoe Co.*, 24 S.W. 580 (Tex. Civ. App. 1893).

⁷¹ *Wiggins v. Blackshear*, 86 Tex. 665, 26 S.W. 939 (1894); *Tom v. First Nat'l Bank*, 104 S.W.2d 130 (Tex. Civ. App. 1937) error dism.; *Luck v. Hopkins*, 54 S.W. 429 (Tex. Civ. App. 1899) error dism.

⁷² See *Egan v. American State Bank*, 67 S.W.2d 1081, 1085 (Tex. Civ. App. 1934) error ref.

⁷³ See *Wiggins v. Blackshear*, 86 Tex. 665, 670, 26 S.W. 939, 940-41 (1894).

⁷⁴ *Willis v. Satterfield*, 85 Tex. 301, 20 S.W. 155 (1892); *Willis v. Heath*, 18 S.W. 801 (Tex. 1891); *Stansell v. Fleming*, 81 Tex. 294, 16 S.W. 1033 (1891); *Sanchez v. Goldfrank*, 27 S.W. 204 (Tex. Civ. App. 1894).

The seller's equitable lien and the creditor's quasi-liens are lost even if the purchasing partner agrees to pay all the partnership debts, unless the selling partner reserves the right to have the partnership property applied to the payment of partnership debts. *Stansell v. Fleming*, supra; *Hart v. Blum*, 76 Tex. 113, 13 S.W. 181 (1890); *Sanchez v. Goldfrank*, supra.

solvent. Once the assets become separate property, however, the partnership creditors lose their priority and are only entitled to share pro rata with separate creditors so far as that property is concerned.⁷⁵

Removal of partnership assets from the business in any of the above ways, with the resultant loss by the partnership creditors of their quasi-liens therein, does not impair the rights of such creditors too seriously if the partnership is solvent. So long as the partnership is neither insolvent nor thereby rendered insolvent, any such disposition of specific partnership property by the partners will not injure partnership creditors, except to the extent that it reduces the margin of safety of partnership assets in excess of liabilities. Transfer of partnership property to a third person or a partner without an equal amount of new assets being received by the partnership made at a time when the firm is insolvent, however, may seriously injure partnership creditors unless the transfer can be set aside.⁷⁶ Under the Texas fraudulent conveyance statute only transfers made with an "intent to delay, hinder or defraud creditors," or voluntarily made by an insolvent debtor "not upon consideration deemed valuable in law," are void as against prior creditors.⁷⁷ It has been held, however, that a conveyance or mortgage of his share of partnership property by a partner in an insolvent partnership with the consent of his co-partners, made to pay or secure his individual debts, is not fraudulent as to partnership creditors.⁷⁸ Likewise, the Texas courts hold that the pay-

⁷⁵ *Roberson v. Tonn*, 76 Tex. 535, 13 S.W. 385 (1890); *Higgins v. Rector*, 47 Tex. 361 (1877). See *Webb v. Gregory*, 108 S.W. 478, 479 (Tex. Civ. App. 1908).

⁷⁶ In determining whether the partnership is insolvent, the solvency of the partners must be taken into account, since their separate property can be reached by the partnership creditors. See note 93 *infra*. If the partners have sufficient surpluses of assets in excess of their separate debts to equal a deficit in the partnership accounts, the partnership is not insolvent. See note 214 *infra*. Thus, if the partners who withdraw partnership property and add it to their separate property are not insolvent, the solvency of the partnership and the rights of the partnership creditors will not be immediately affected by a transfer of partnership assets to the partners. Of course, there is always the danger that the partners who acquire the partnership property will dispose of it without receiving fair consideration therefor, or will become insolvent, and thus the partnership creditors would prefer to have the partnership assets remain in the business.

⁷⁷ Tex. Rev. Civ. Stat. arts. 3996-3997 (1925).

⁷⁸ *Wiggins v. Blackshear*, 86 Tex. 665, 26 S.W. 939 (1894) (holding that the partners of an insolvent partnership can lawfully permit each other to pay individual debts out of their respective shares of the partnership property. ". . . [A]lthough the firm be insolvent, partners by mutual agreement may, within the limit heretofore noticed, prefer individual creditors, if this be done in good faith." *Wiggins v. Blackshear*, *id.* at 671, 26 S.W. at 941); see also *Watts v. Debois*, 66 S.W. 698 (Tex. Civ. App. 1902); *Texas Drug Co. v. Baker*, 50 S.W. 157 (Tex. Civ. App. 1899) error ref.; *Batchelor v. Sanger*, 38 S.W. 359 (Tex. Civ. App. 1896).

The Supreme Court of Texas has also said that where an insolvent partnership is dissolved and the property divided among the partners according to their interests, the trans-

ment by an insolvent debtor, including a partnership, of the claims of one or more of its creditors does not, within the meaning of the fraudulent conveyance statute, hinder, delay, or defraud the other creditors simply because it prefers the creditors paid.⁷⁹ Moreover, where the partnership is solvent, it has been held that a sale by one partner to his co-partner of all his interest in the partnership assets, the purchasing partner assuming liability for all partnership debts, could not hinder, delay, or defraud partnership creditors, who by proceeding against the purchasing partner could reach the property through judgment and execution.⁸⁰ Even if the partnership is insolvent, such a sale is not necessarily fraudulent against the partnership creditors, it being necessary for the creditors to show a primary intent to hinder, delay, or defraud the creditors.⁸¹

Thus, under present Texas law creditors of an insolvent partnership are not always entitled to have set aside preferential transfers to separate or other partnership creditors, or transfers of property to a partner. While a more stringent Texas fraudulent conveyance statute might be desirable,⁸² the present law is not too damaging to the creditors of an insolvent partnership in light of the availability to them of the National Bankruptcy Act,⁸³ under which the trustee in bankruptcy can set aside the above kind of transfers.⁸⁴

action is not of itself fraudulent as against partnership creditors since "the property in the hands of each partner would be subject, as before, to the claims of partnership creditors as well as others." *Wiggins v. Blackshear*, supra at 670, 26 S.W. at 941. This proposition seems to overlook the fact that removal of the property from the partnership may very well hinder or delay partnership creditors, who by the removal lose their priority vis-a-vis separate creditors.

⁷⁹ *Haas v. Kraus*, 86 Tex. 687, 27 S.W. 256 (1894); *Ellis v. Vallentine*, 65 Tex. 532 (1886) (extensive discussion of "hinder" and "delay" as those terms are used in the fraudulent conveyance statute); *Chesher v. Clamp*, 30 S.W. 466 (Tex. Civ. App. 1895).

⁸⁰ *Stansell v. Fleming*, 81 Tex. 294, 16 S.W. 1033 (1891). This proposition is subject to the same defect referred to in note 78 supra.

⁸¹ See *Sanchez v. Goldfrank*, 27 S.W. 204, 207 (Tex. Civ. App. 1894).

⁸² Greater protection is given partnership creditors by the Uniform Fraudulent Conveyances Act, not in force in Texas, § 8 of which reads as follows:

Every conveyance of partnership property and every partnership obligation incurred when the partnership is or will be thereby rendered insolvent, is fraudulent as to partnership creditors, if the conveyance is made or obligation incurred,

(a) To a partner, whether with or without a promise by him to pay partnership debts, or

(b) To a person not a partner without fair consideration to the partnership as distinguished from consideration to the individual partners.

Although "fair consideration to the partnership" is not defined, it would seem that there is no "fair consideration" when partnership assets are used to pay or secure a partner's separate obligation, but that there is when they are used to pay or secure a partnership debt, even though such transfer might constitute a preference. See *Crane, Partnership* § 46 (2d ed. 1952).

⁸³ 30 Stat. 544 (1898), as amended, 11 U.S.C. §§ 1-1103 (1952).

⁸⁴ Under § 60(b) of the National Bankruptcy Act, the trustee may avoid any "preference" and recover the property if the creditor receiving it had, at the time of the transfer, reasonable cause to believe that the debtor was insolvent. 11 U.S.C. § 96(b)

No provision as to the validity of such transfers is made in the Uniform Partnership Act, which relies on the local law of fraudulent conveyances and the bankruptcy act to protect the creditors of an insolvent partnership.⁸⁵ The act, however, does give partnership creditors one kind of protection which they do not have under present Texas law by denying to the partners, as against partnership creditors, any right under the homestead or exemption laws in partnership property attached for a partnership debt.⁸⁶

The position of the partnership creditor is much more precarious in another situation, that in which the partnership is dissolved by the retirement or addition of a partner and the business is carried on by a new partnership without liquidation of the partnership affairs. This situation can arise when a partner with the consent

(1952). A preference is defined in § 60(a)(1) of the National Bankruptcy Act, 11 U.S.C. § 96(a)(1), as "a transfer . . . of any of the property of a debtor to or for the benefit of a creditor for or on account of an antecedent debt, made or suffered by such debtor while insolvent and within four months before the filing by or against him of the petition initiating a proceeding under this Act, the effect of which transfer will be to enable such creditor to obtain a greater percentage of his debt than some other creditor of the same class." In addition, § 70(e)(1) declares null and void as against the trustee any transfer which is fraudulent under any federal or state law applicable thereto. 11 U.S.C. § 110(e)(1) (1952). Section 67(d)(4), 11 U.S.C. § 107(d)(4) (1952), provides: "Every transfer of partnership property and every partnership obligation incurred within one year prior to the filing of a petition initiating a proceeding under this Act by or against the partnership, when the partnership is insolvent or will be thereby rendered insolvent, is fraudulent as to partnership creditors existing at the time of such transfer or obligation, without regard to actual intent if made or incurred (a) to a partner, whether with or without a promise by him to pay partnership debts, or (b) to a person not a partner without fair consideration to the partnership as distinguished from consideration to the individual partners." Transfers made within one year of bankruptcy "without fair consideration by a debtor who is or will be thereby rendered insolvent," or made "with actual intent . . . to hinder, delay or defraud" creditors, are declared fraudulent by § 67(d)(2), 11 U.S.C. § 107(d)(2) (1952).

In spite of the broad protection afforded partnership creditors by the National Bankruptcy Act, those who are unable or unwilling to proceed thereunder could very well be adversely affected by the gaps in the Texas fraudulent conveyance statute, as interpreted by the Texas courts.

⁸⁵ See Crane, *supra* note 59, at 774-76, criticizing the act for its failure to deal with this subject. An earlier draft of the act did contain a fraudulent conveyances section, which read as follows:

Seventh Draft. Sec. 21. (Fraudulent Conveyances.) (1) Every conveyance or encumbrance of partnership property by a partner made or given voluntarily and without a present and fair consideration to the partnership, as distinguished from a consideration to the individual members, when the partnership is or will be thereby rendered insolvent or in contemplation of insolvency, shall be void as against the partnership creditors, except as to purchasers in good faith and for a present fair consideration.

(2) Every conveyance or encumbrance of partnership property, every obligation incurred and every judicial proceeding taken by any partner, with intent to hinder, delay, or defraud any partnership creditor, or other person, of his demand against the partnership or which will have this effect, is void as against the partnership creditors, except as to purchasers in good faith and for a present fair consideration.

(3) Under the provisions of this section every conveyance or encumbrance of partnership property by any partner, to any partner made when the partnership or the assignee partner is insolvent, is void as against the partnership creditors, whether such insolvency be known to the partners or not. *Ibid.* See note 91 *infra*.

⁸⁶ § 25(2)(c). Of course, under § 25(2)(b) all the partners could assign specific partnership property to one of the partners, who could then fasten a homestead exemption

of his co-partners sells his interest in the partnership or all the partnership property to a third person (or to one or more of his co-partners and a third person), when there are three or more partners and one sells his interest to the others, or when the partners admit a new partner into the business. In all these cases the first partnership is dissolved;⁸⁷ and if the business is continued without liquidation of the affairs of the partnership, the assets become the property of the new partnership, and the equitable lien of the seller and the quasi-liens of the creditors of the first partnership are lost.⁸⁸ Of course, the creditors of the first partnership continue as creditors of the members of that firm,⁸⁹ but they are not regarded as creditors of the new partnership; and the creditors of the new partnership have priority as to its property, including that which originally belonged to the first partnership.⁹⁰ The practical result is that the claims of the creditors of the first partnership may not be satisfied even though at the time of its dissolution it may have been solvent and the business may have been continued without

upon it. In order to do so, however, the property would have to be removed from the business, which the other partners might be unwilling to do.

It is not clear in Texas whether the other family exemptions, beside the homestead exemption, provided for in art. 3832, Tex. Rev. Civ. Stat. (1925), such as that for tools of a trade, prevent partnership creditors from reaching such property. *B. C. Evans Co. v. Kingsbury*, 25 S.W. 729 (Tex. Civ. App. 1894), holds that one partner cannot make partnership property exempt from attachment by partnership creditors, as household goods, by placing the property in his house. In that case, however, it is not made clear whether the rights of the partnership creditors are dependent upon the equitable liens of the other partners; if so, such an exemption could be accomplished if all the partners consent to the removal of the property from the partnership. The court did state that if partnership property is sold by the firm to a partner with the intent to delay, hinder, or defraud partnership creditors, the sale is void; this statement seems to imply that a partner may, with the consent of his co-partners, remove partnership property and use it in such a way as to exempt it from attachment by partnership creditors, if there is no intent to delay, hinder, or defraud the creditors.

⁸⁷ See note 55 *supra*. Cf. *Dillard v. John Chatmas Wholesale*, 286 S.W.2d 675 (Tex. Civ. App. 1956) (stating, with some confusion of thought, that a sale of a partnership interest without compliance with the Bulk Sales Law, Tex. Rev. Civ. Stat. Ann. art. 4001 (1945), rendered the continuing partnership liable for the debts of the prior partnership).

⁸⁸ *Hawkins v. Western Nat'l Bank*, 146 S.W. 1191 (Tex. Civ. App. 1912); *Bell v. Beazley*, 45 S.W. 401 (Tex. Civ. App. 1898).

Even if the partnership is insolvent at the time one partner sells his interest to a third person, so that its effect may be to hinder or delay creditors of the partnership, the sale is not void as a fraudulent conveyance so long as it was real, and not simulated, and was not made for the purpose of defrauding the partnership creditors. *Bell v. Beazley*, 45 S.W. at 402.

⁸⁹ *White v. Boone*, 71 Tex. 714, 12 S.W. 51 (1888); *Frost v. First State Bank & Trust Co.*, 276 S.W. 222 (Tex. Comm. App. 1925). They also continue as creditors of the first partnership, but this position will ordinarily do them no good since all of the property of that partnership has become the property of the new partnership.

⁹⁰ Cases cited note 88 *supra*; *Lewis*, *supra* note 56, at 635.

A promise by the new partner to assume the liabilities of the old partnership does not preserve the quasi-liens of the creditors of that partnership; it merely gives them a personal claim against the new partner. *Bell v. Beazley*, 45 S.W. 401 (Tex. Civ. App. 1898).

any notice to the creditors of the change in make-up of the partnership.

This inequitable result is eliminated by section 41 of the act, which proceeds upon the theory that all rights of partnership creditors in partnership property should not be lost merely because of a change in the membership of the firm, if the business is carried on without liquidation of the debts of the dissolved partnership.⁹¹ To that end, section 41(1) provides that when such a change takes place without liquidation of the affairs of the partnership, either by the admission of a new partner or the retirement or death of a partner and the assignment of his interest to some or all of those continuing the business, the creditors of the dissolved partnership become creditors of the partnership continuing the business. The effect of section 41(1) is that the creditors of the first partnership do not lose their quasi-liens on the partnership property, but rather are given an equal claim on the property of the new partnership with those who extend credit after the dissolution of the first partnership caused by a change in personnel.⁹² Section 41(2) provides a corresponding solution for the situation in which all the partners assign their interests to one partner, who continues the business without liquidation of partnership debts; it makes partnership creditors separate creditors of the partner continuing the business (and of the partnership if the remaining partner takes in one or more new partners), whether he promises to pay the debts of the dissolved partnership or not.⁹³

⁹¹ "The paragraph as a whole, as well as this entire section, is based on the opinion that when there is a continuous business carried on first by A, B and C, and then by A, B, C and D, or by B or C, or by B and C, by B and D, or by C and D, or by B, C and D, without any liquidation of the affairs of A, B, C, both justice and business convenience require that all the creditors of the business, irrespective of the exact grouping of the owners at the times their respective claims had their origin, should be treated alike, all being given an equal claim on the property embarked in the business." Commissioners' Note to § 41.

⁹² Another possible approach to this problem would have been to declare the transfer of property from the first partnership to the new one a fraudulent conveyance and thus void as against the creditors of the first partnership. This approach was not adopted since the effect of re-transferring the property to the first partnership is to deprive creditors of the new partnership of any claim to such property until the creditors of the first partnership are paid in full, thus placing the new creditors "in as hard a position as that from which the creditors of the first partnership have been relieved by the court's action." Lewis, *supra* note 56, at 636. The act has been criticized for letting in new creditors on a parity with the old creditors. Crane, *supra* note 59, at 778. It would seem, however, that the act's solution of this problem is a sensible one since it is based on the realistic attitude that there is really only one continuous business, even though there has been some change in the group of partners conducting it. Thus, the new creditors as well as the old must be allowed to share in the partnership property, just as they would have had there been no change in the personnel of the partnership at the time they extended credit.

⁹³ Section 41(2) would not, in effect, change the existing Texas law in regard to the liability of the separate estate of the remaining partner for unsatisfied partnership debts. The Texas cases do not give separate creditors priority over partnership creditors in the separate estates of the partners, as does § 40(h), (i) of the act. Rather, they hold that a

In order for the policy of section 41 to be carried out where a third person is admitted into a going business as a partner, it is, of course, necessary that the incoming partner be liable for the existing debts of the partnership, to the extent of his interest in the partnership property. It is so provided in section 17 of the act, and the principle is reiterated in section 41(7).⁹⁴

D. Rights of Separate Creditors in Partnership Property

Assignment by a partner of his interest in the partnership is not the only way in which the rights of the other partners may be disturbed under the present Texas law.⁹⁵ The same problem is presented when a partner has been unable to pay his individual debts, and one of his creditors attempts to attach or levy execution upon the debtor partner's interest in partnership property. If separate creditors were permitted to seize partnership property on attachment or execution, the partnership business would be subject to crippling interruptions which would injure not only the debtor partner, but all of the others.

This problem has been recognized in Texas and has been partially solved by rule 642 of the Rules of Civil Procedure,⁹⁶ which provides that a levy on a partner's interest in partnership property can be made only by leaving notice of the levy with one or more of the partners or with a clerk of the partnership.⁹⁷ The courts

partner's separate property is equally liable for partnership debts and personal obligations. See cases cited note 75 *supra*. Of course, by making creditors of the dissolved partnership creditors of the new partnership where the remaining partner and others continue the business without liquidation of the old partnership's affairs, § 41(2) does change the existing law.

Professor Crane has criticized § 41(2) because it allows all the separate creditors to come in on a parity with the creditors of the dissolved partnership. Crane, *supra* note 59, at 778. This criticism clearly has merit, at least with respect to the claims of those who became separate creditors of the purchasing partner before the assignment to him of the partnership property. They, unlike subsequent creditors who would have extended credit to the old partnership had it not been dissolved, would have been subordinated to the claims of the partnership creditors in the partnership property had the firm been continued without change in personnel.

⁹⁴ Sections 17 and 41, by subjecting the incoming partner's interest in partnership property, including that acquired after his admission, to liability for the debts of the old partnership, would change the present Texas law, under which an incoming partner has no liability for debts already incurred in the absence of an agreement to that effect. *Freeman v. Huttig Sash & Door Co.*, 105 Tex. 560, 153 S.W. 122 (1913). Sections 17 and 41(7) do not, however, give the creditors of the first partnership any right in the incoming partner's separate estate, which can only be reached by those partnership creditors who extend credit after his admission.

⁹⁵ See notes 55-57 *supra* and accompanying text.

⁹⁶ Rule 642 was formerly embodied in art. 2295, Tex. Rev. Civ. Stat. (1925). Rule 642 deals expressly only with levy of execution. Rule 598, however, provides: "The writ of attachment shall be levied in the same manner as is, or may be, the writ of execution upon similar property."

⁹⁷ Garnishment for the separate debt of a partner does not present the same problem of

have given teeth to this rule by holding that if a separate creditor violates it by having an officer seize physical possession of partnership property, the creditor and the officer are both guilty of conversion.⁹⁸ Rule 642, however, does not completely insulate the partnership assets from separate creditors, for after a separate creditor has levied upon the debtor partner's interest in the partnership, he may cause that interest to be sold at execution sale,⁹⁹ and the purchaser can realize on the interest by bringing an action for an accounting.¹⁰⁰ Such action by the purchaser, of course, spells the end of the partnership, for it must be wound up and the debtor partner's interest in the surplus distributed to the purchaser at the execution sale. The only way in which the other partners can protect themselves against such a result is either by paying off the separate creditor at the outset and taking over his claim against the debtor partner, or by making the highest bid at the execution sale so that the debtor partner's interest in the partnership does not fall into the hands of outsiders.¹⁰¹

The act, like rule 642, provides as an incident of tenancy in partnership that a partner's right in specific partnership property is not subject to attachment or execution by his separate creditors.¹⁰² Moreover, section 28 provides a much more effective method of protecting the other partners against being disturbed by a separate creditor in their use of partnership property than does rule 642. It establishes an entirely new kind of remedy, called a "charging order," as the exclusive method by which a separate creditor can

disturbance of the rights of the other partners as does attachment or execution. The Texas courts, without the aid of a statute or rule of court, have held that a debt due to the partnership by a third person, or partnership funds in the hands of a third person or the partnership itself, cannot be garnished by a separate creditor for the individual debt of one of the partners. *Barrett v. Craft*, 57 S.W.2d 387 (Tex. Civ. App. 1933); *Belva Oil Co. v. Lowe*, 27 S.W.2d 599 (Tex. Civ. App. 1930); *Brown v. Cassidy-Southwestern Comm'n Co.*, 225 S.W. 833 (Tex. Civ. App. 1920). The reason given is that a partner has no right in specific partnership property, and "that until the settlement of the partnership business it cannot be affirmed that an individual partner has any specific interest that may be appropriated to his individual debt." *Id.* at 835.

⁹⁸ *Middlebrook v. Zapp*, 79 Tex. 321, 15 S.W. 258 (1891); *Leonard v. Worsham*, 45 S.W. 336 (Tex. Civ. App. 1898); *Howell Bros. v. Jones & Owen*, 3 Willson Tex. Ct. of App. (Civ. Cas.) § 208 (1886).

⁹⁹ *J. M. Radford Grocery Co. v. Owens*, 161 S.W. 911 (Tex. Civ. App. 1913).

¹⁰⁰ *Jones v. Meyer Bros. Drug Co.*, 61 S.W. 553 (Tex. Civ. App. 1901) error ref. See *J. M. Radford Grocery Co. v. Owens*, *supra* note 97 at 913; *Donald v. Carpenter*, 27 S.W. 1053, 1055 (Tex. Civ. App. 1894); *Howell Bros. v. Jones & Owen*, 3 Willson Tex. Ct. of App. (Civ. Cas.) § 208 (1886).

¹⁰¹ In most cases, probably the only bidders at the execution sale other than the non-debtor partners will be the separate creditors themselves or speculators engaged in the business of buying such interests at execution sales.

¹⁰² § 25(2) (c).

reach the debtor partner's interest in the partnership.¹⁰³ Under section 28 the separate creditor may, after obtaining a judgment, apply to a court for an order that the interest of the debtor partner be charged with the payment of the judgment debt and interest. The court is empowered to appoint a receiver of the debtor partner's share of the profits and other money due him from the partnership, or to order a sale of the interest charged. In this way the separate creditor's claim can be satisfied without in any way upsetting the business of the partnership or its use of partnership property, and there is no need for the partnership to be dissolved simply because one of the partners is unable to meet his separate debts.¹⁰⁴

E. Acquisition and Transfer of Real Property in Partnership Name

One of the most serious areas of uncertainty created by the application of traditional common-law rules of ownership to partnership property is that having to do with the ownership of partnership real property. Since at common law title to real estate can only be held by recognized legal persons,¹⁰⁵ and since at common law a partnership is treated as an aggregate of the partners rather than as a separate legal entity,¹⁰⁶ it must follow that a partnership cannot take title to real estate in its firm name. And in Texas a conveyance to or by a partnership in the partnership name does not as a general rule pass the legal title to the property.¹⁰⁷ Such a principle can only result in confusion, since in the business world a partnership is thought of as a separate entity capable of owning real property, and frequently conveyances are made in its name. The confusion has been increased by cases holding that if the name of one or more partners is contained in the name of the partnership, legal

¹⁰³ The charging order of § 28 was derived from the English Partnership Act, Partnership Act, 1890, 53 & 54 Vict. 229, c. 39. Section 28 has recently been analyzed by Gose, *The Charging Order Under the Uniform Partnership Act*, 28 Wash. L. Rev. 1 (1953), and in Note, *Charging Orders Under the Uniform Partnership Act*, 9 Wyo. L.J. 112 (1955).

¹⁰⁴ Section 28(2) provides that the sale of the interest charged will not automatically cause a dissolution. Under § 32(2), however, the purchaser of a partner's interest may obtain a dissolution by decree of court after the termination of the specified term of the partnership or at any time if the partnership was a partnership at will when the charging order was issued. See note 66 *supra*.

¹⁰⁵ See *Dunlap v. Green*, 60 Fed. 242, 246 (5th Cir. 1894); *Crane, Partnership* § 38 (2d ed. 1952).

¹⁰⁶ See note 31 *supra*.

¹⁰⁷ See *Dunlap v. Green*, 60 Fed. 242, 246-47 (5th Cir. 1894); *Frost v. Wolf*, 77 Tex. 455, 460-61, 14 S.W. 440, 441-42 (1890); *Baldwin v. Richardson & Co.*, 33 Tex. 16, 30 (1870); *Harris v. Bryson & Hartgrove*, 80 S.W. 105, 106 (Tex. Civ. App. 1904) error ref. But see *Hollingsworth v. Wm. Cameron & Co.*, 160 S.W. 644 (Tex. Civ. App. 1913) (holding that deed to "B. P. Hollingsworth & Bro." passed legal title to one-half interest in the land to each of the two partners).

title passes to those partners, who hold it in trust for the partnership.¹⁰⁸ Since only a few cases have arisen in which the exception has been applied, there remains great uncertainty as to when the name of a partner is sufficiently identified in the name of the partnership so that the courts will hold that legal title passes to him in trust for the partnership.¹⁰⁹

The great inequity that could result from a holding that a partnership which has paid value for land taken in its name, or a purchaser from a partnership, does not acquire legal title has been largely obviated by the holding of the courts that even though legal title does not pass, equitable title does.¹¹⁰ Equity can therefore see that justice is done by requiring the holder of the legal title to convey it to the party or parties entitled thereto. There still remain, however, the problems of the cloud on the title which appear every time the name of a partnership is in a chain of title; the time, trouble, and expense involved in removing such clouds; the possibility that the holder of the legal title will make a conveyance that cuts off equities before he is forced to convey legal title to the equitable owners; the practical difficulty that a potential purchaser of partnership real property faces in deciding whom he should insist sign the deed as grantors.¹¹¹

The act eliminates these problems by providing in section 8(3) that any estate in real property may be acquired in the partnership name, and that title so acquired can be conveyed only in the partnership name. Moreover, it also eliminates the uncertainty as to what kind of title passes when partnership property acquired in the firm name is not conveyed in the firm name, or when property not acquired in the firm name is conveyed by one or more of the partners. Section 10 makes detailed provision as to what title passes when title is in the partnership name and a partner conveys

¹⁰⁸ *Lindsay v. Jaffray*, 55 Tex. 626 (1881) (deed to "E. S. Jaffray & Co." passed legal title to E. S. Jaffray in trust for the partners composing the firm); *Gauss-Langenburg Hat Co. v. Allums*, 184 S.W. 288 (Tex. Civ. App. 1916) error ref. (deed to "C. R. Hooks & Co." passed legal title to C. R. Hooks in trust for the partnership).

¹⁰⁹ For example, what would have been the result in *Gauss-Langenburg Hat Co. v. Allums*, supra note 108, had the conveyance been made to "C. R. Hooks Co." or "Hooks & Son"? Would the Texas courts hold that legal title passed to C. R. Hooks, or to Hooks and his son, in trust for the partnership?

¹¹⁰ *Dunlap v. Green*, 60 Fed. 242 (5th Cir. 1894); *Frost v. Wolf*, 77 Tex. 455, 14 S.W. 440 (1890); *Baldwin v. Richardson & Co.*, 33 Tex. 16 (1870); *Harris v. Bryson & Hartgrove*, 80 S.W. 105 (Tex. Civ. App. 1904) error ref.

¹¹¹ The safest course for a purchaser to follow is to require that all the partners sign as grantors, which should protect him if legal title is in one or more of them, or in one or more of them in trust for the partnership. However, if legal title never passed to any of the partners, or if the name of a partnership appears earlier in the chain of title, the purchaser might still be faced with the problems mentioned.

in his own name; when title is in the name of some, but not all, of the partners, the record not disclosing the right of the partnership, and those partners convey; when title is in the name of one or more partners, or a third person in trust for the partnership, and a partner conveys in the partnership or his own name; and when title is in the name of all the partners and they all execute a conveyance. Thus, the act eliminates the confusion and uncertainty with respect to the conveyance of real property belonging to a partnership that exist under the common law and the present law of Texas.

III. RELATIONS AMONG PARTNERS

There is no public need for regulation of the internal relations among partners comparable to the need for imposing liability on an ostensible partner or prescribing detailed rules for corporations as the price of limited liability. Traditionally, partners' relations with one another have been matters for private agreement, subject only to the law of contracts. Should legislation attempt to regulate these relations? If it does not, what point is there in having a statute? These questions were wisely answered by the framers of the Uniform Act. They concluded not to supplant private agreement in determining partner's relations *inter se*.¹¹²

The drafter of partnership agreements has no less importance under the act than at common law, but his services will probably be confined generally to the more elaborate business associations for which the rather rudimentary provisions of the act are insufficient. The act will, however, be of great value as a reference, for it is surprising how many formal agreements are drawn, heedless of substantive law, to achieve particular results under the intricacies of the partnership provisions of the federal tax laws.¹¹³ The act operates whenever the partners have failed to make a meaningful agreement on the subject in question. When all partnerships have clear and comprehensive written agreements, the act (and the courts) will scarcely be necessary. Until then, the act offers coherence and precision that have not always been available in the Texas decisions, mired as they are in dicta.

The ensuing discussion assumes that the partners have made no agreement relevant to the disputed issues.

¹¹² § 18 (first clause).

¹¹³ Int. Rev. Code of 1954, §§ 701-71.

A. Profits, Losses, and Capital

The essence of partnership is profit sharing. In general, the partners share equally, even though they may have contributed unequally to capital.¹¹⁴ The obligation to share losses is a corollary of the "community of interests" which gives the right to share profits.¹¹⁵ The partners share losses in the same proportions as they share profits, even though they may have contributed to capital in different proportions.¹¹⁶

Implicit in sharing is the question of what is to be shared. There is little doubt that profits (*i.e.*, net profits) of ordinary business operations are to be shared.¹¹⁷ Dispute, however, may arise with respect to what are loosely called "capital" losses. The matter is somewhat confused and may perhaps best be analyzed in terms of the various arguments advanced.

1. Loss of a Particular Asset

The loss may be associated with a particular asset, *i.e.*, the asset has been sold below cost. In this event, it is necessary to know whether the asset belonged to the partnership or to one or more of the partners individually.¹¹⁸ For illustration, suppose partner X brings to the partnership a herd of cattle. It is understood that the cattle will be grazed and ultimately sold, at which time the profits will be divided. If the cattle should be sold at a loss, X's co-partners may argue that the cattle, hence the loss, belonged to X alone and not to the partnership.¹¹⁹ More specifically, their position is that X contributed the "use" but not the "property" of the asset to the partnership. This, they say, would not entitle them to share in the asset if it remained intact, hence should not obligate them to share

¹¹⁴ Johnston v. Ballard, 83 Tex. 486, 18 S.W. 686 (1892) (dicta). There is even Texas language to the effect that a partner's failure to contribute his promised capital does not deprive him of the right to share profits, First Nat'l Bank v. Rush, 246 S.W. 349 (Tex. Comm. App. 1922), although it is hard to see why this is not a material failure of consideration. Cf. Werner v. Mitchell, 2 S.W.2d 477 (Tex. Civ. App. 1928) error dism. (profits recoverable by partner must be reduced by amount he promised but failed to contribute to partnership).

¹¹⁵ Bivins v. Proctor, 125 Tex. 137, 80 S.W.2d 307 (1935).

¹¹⁶ Paggi v. Quinn, 179 S.W.2d 789 (Tex. Civ. App. 1944), error ref. w.o.m.

¹¹⁷ Partners may agree to share gross proceeds without equalizing their respective outlays and expenses. See Whitis v. Polk, 36 Tex. 602 (1872).

¹¹⁸ The earliest Texas discussion suggests—misleadingly in light of later law—that the partner's joint ownership of the asset is the basis for sharing expenses or losses in respect of it. *Id.* at 623.

¹¹⁹ Johnston v. Steele, 107 S.W. 631 (Tex. Civ. App. 1908). The same argument, in the event of a gain, shows that the gain belongs entirely to X. Hatzfield v. Walsh, 120 S.W. 525 (Tex. Civ. App. 1909) error ref. The incompatibility of the gain argument with the profit sharing purposes of partnership suggests the invalidity of the loss argument.

in it if it is impaired (sold unprofitably).¹²⁰ The weakness of this argument is that the co-partners would not share in the asset even if its "property" had been contributed to the partnership.¹²¹

The question whether the partnership had the "property" or merely the "use" of an asset may arise if the asset was once owned individually by X or if it was purchased with funds furnished by him. The answer is complicated by the legal doubt which characterizes the ownership of realty by a partnership and the normal informality which characterizes the handling of personalty by close associates. The courts attempt to answer the question by inferring the intent of the partners as to whether the asset was to be partnership property.¹²² If the asset is of the kind normally traded or consumed by the partnership, there is some reason to assume that putting it at the disposal of the partnership was an act intended to make it partnership property.¹²³ This view does not prevent assets of a different kind from becoming partnership property if the requisite intent can be found; the presumption of firm ownership is, however, weaker. Evidence of intent may be found in the terms of the partnership agreement, in the way the asset is treated on partnership records and financial statements, or in the behavior of the partners with respect to it.

Besides the "use" theory, the "labor" theory needs to be considered. It often happens that while X has contributed assets to the partnership, his co-partner Y has furnished only labor.¹²⁴ Y then has the additional argument that his labor counterbalances X's assets as a contribution to the partnership; Y suffers the loss of his labor just as much as X suffers the loss of his assets; therefore

¹²⁰ *Masterson v. Allen*, 29 S.W.2d 539, 542-43 (Tex. Civ. App. 1934) error ref.

¹²¹ See note 144 *infra* and accompanying text.

¹²² *Johnston v. Steele*, 107 S.W. 631 (Tex. Civ. App. 1908), as explained in *Paggi v. Quinn*, 179 S.W.2d 789, 795 (Tex. Civ. App. 1944) error ref. w.o.m. (construing written contract). The question is not, of course, peculiar to Texas; see Annot., 45 A.L.R.2d 1009 (1956). A similar question arises in connection with the distribution of assets on dissolution and with conflicting priorities of individual and partnership creditors. The determination is one of fact, reached in the same general way described in the text. See *Murrell v. Mandelbaum*, 85 Tex. 22, 19 S.W. 880 (1892) (land belonged to partnership, not to partners as tenants in common, when it was acquired during partnership and in partnership name and "was regarded by them as a part of the partnership stock"), *Luck v. Hopkins*, 54 S.W. 429 (Tex. Civ. App. 1899) error ref. (mill property belonged to partnership when it was used and operated to carry on the partnership business, was bought with a view to this purpose, and was paid for by profits arising from the partnership).

¹²³ Cf. *Bradford v. Bradford*, 172 S.W.2d 365, 367 (Tex. Civ. App. 1943) (property consumed); *Bivins v. Proctor*, 125 Tex. 137, 152-53, 80 S.W.2d 307, 315 (1935).

¹²⁴ The related question of compensation for services and interest on capital is discussed in notes 156-76 *infra* and accompanying text.

neither should contribute to the other's loss.¹²⁵ This theory affords no guidance if the loss exceeds X's asset contribution. Moreover, the reasoning is specious if value is gauged by future earning power: that of X's asset is lost with the asset, that of Y's labor continues as a personal capacity. It is not wholly unreasonable, of course, to conclude that no sharing of losses is intended if one partner furnishes all of the assets and the other all of the labor. However, such a conclusion conflicts with the fundamental "community of interests" principle and should be reached only by way of a factual finding of partners' intent¹²⁶ and not by legal generalization.

The leading Texas case¹²⁷ has impliedly recognized the validity of both the "use" and the "labor" theories. It suggests that the first will apply only to fixed assets¹²⁸ and the second only if there is an affirmative agreement,¹²⁹ and that the courts will be reluctant to accept either.¹³⁰ These two theories constitute exceptions to the general rule that partners must share *all* losses, which is the logical derivation of the "community of interests" that entitles each to share profits¹³¹ and makes each fully liable to third persons.¹³²

Most often the "use" and "labor" theories are mentioned when the asset which is disposed of at a loss is "capital" in the sense of a fixed asset, as distinguished from inventory.¹³³ Texas courts have not voiced precisely this idea but it seems to underly their concern with whether the loss is of partnership "capital"; here "capital" ap-

¹²⁵ *Bivins v. Proctor*, 125 Tex. 137, 139-40, 145, 80 S.W.2d 307, 308, 311 (1935). See also *Masterson v. Allen*, 69 S.W.2d 539 (Tex. Civ. App. 1934) error ref., applying the "labor" theory where only the "use" of the asset (money) was contributed by X. The first of these cases speaks of Y's labor as a contribution to partnership "capital" despite the complete contradiction in terms. Insofar as the "labor" theory tends to limit a partner's loss to his economic contribution, it is echoed in the federal tax provisions employing a partner's basis as the limit on deductibility of his share of partnership losses. Int. Rev. Code of 1954, §§ 704(d), 705(a), 722, 752(a).

¹²⁶ Cf. *Simpson v. Fulcher*, 45 S.W.2d 1012 (Tex. Civ. App. 1931) error ref. (agreement to share profits; jury finding of no joint ownership of goats supported holding that there was no obligation to share loss on sale of goats).

¹²⁷ *Bivins v. Proctor*, 125 Tex. 137, 80 S.W.2d 307 (1935).

¹²⁸ *Id.* at 152-53, 80 S.W.2d at 315.

¹²⁹ *Id.* at 145, 80 S.W.2d at 311.

¹³⁰ *Ibid.*; accord, *Paggi v. Quinn*, 179 S.W.2d 789 (Tex. Civ. App. 1944) error ref. w.o.m.

¹³¹ *Bivins v. Proctor*, 125 Tex. 137, 80 S.W.2d 137 (1935); *Paggi v. Quinn*, *supra* note 130.

¹³² A third person may recover against any or all of the partners regardless of the agreement among the partners as to sharing of losses. *Miller v. Marx*, 65 Tex. 131 (1885) (void agreement); *Asch v. First Nat'l Bank*, 304 S.W.2d 179 (Tex. Civ. App. 1957) error ref. n.r.e.; *Davis v. Gilmore*, 244 S.W.2d 671 (Tex. Civ. App. 1951) error ref. (no agreement as to sharing losses); *Sturdevant v. Hooper*, 101 S.W.2d 379 (Tex. Civ. App. 1947) error dism. (one partner to bear all losses).

¹³³ Cf. Int. Rev. Code of 1954, § 1221.

parently has the connotation of property owned by the partnership and used (but not traded) in its business.¹³⁴

2. Losses of a General Nature

Similar problems may be encountered if the loss is not associated with any particular asset. Here the loss is of X's capital in that the value of partnership assets has been reduced below the value of X's "capital" contribution to the partnership, thereby making it impossible for him to recover his "capital."

The "labor" theory would appear to merit the same scope here that it has with respect to losses on the disposition of a particular asset; but, surprisingly, the "use" theory appears again in this context by way of dictum in one case¹³⁵ and a possible holding in another¹³⁶ that a loss of money need not be shared since the partnership had only the "use" of the money. In the former case the "use" theory was distinguished factually, not repudiated doctrinally; in the latter case it was recited enthusiastically. Thus it appears to have sufficient currency to warrant examination of its two serious defects. First, aside from physical destruction, it cannot be said that this particular money was lost. It was merely paid out for debts and expenses of the partnership. A loss in these circumstances is simply a negative income unrelated to any specific asset. Second, it is difficult to conceive furnishing only the "use" of a commodity so undifferentiated and labile as money.¹³⁷ If the partnership took the money subject to a stronger repayment obligation than attends a partner's capital contribution, it is hard to see how the transaction was anything but a loan.¹³⁸ The responsibility to re-

¹³⁴ *Paggi v. Quinn*, 179 S.W.2d 789, 794 (Tex. Civ. App. 1944) error ref. w.o.m. ("capital" consisted of lease and equipment, not money furnished by one partner for their acquisition).

¹³⁵ *Paggi v. Quinn*, supra note 134 ("use" argued but not proved).

¹³⁶ *Masterson v. Allen*, 69 S.W.2d 539, 542 (Tex. Civ. App. 1934) error ref. The unintelligibility of the court's remarks on this point is demonstrated by the following passage which may constitute an alternative ground for the holding that the asset partner cannot recover from the labor partner:

Neither could any contribution to the debts the notes were claimed to evidence be required of the appellee under any other form, because, as presaged supra, they were all (if in fact any by the partnership) indisputably, if not undisputedly, shown from both the pleadings and the proof to have been losses only of the moneys as capital that were wholly—under the specific conditions already shown—furnished by the appellant alone, wherefore his sole partner, having never owned any individual interest therein, could not be held for the replacement thereof, he only, by well-settled authority, having to bear the total loss.

¹³⁷ *Crane*, *Partnership* § 65 (2d ed. 1952) offers the additional observations that great disparities are unusual but controllable by agreement, and that labor partners are generally execution proof.

¹³⁸ Note, 24 Colum. L. Rev. 508, 511-12 (1924).

pay the loan would not be diminished because of unprofitable use of the loan proceeds. At worst, X would lose his right to collect from his co-partners because of defective pleadings (*e.g.*, alleging loss rather than loan) which could not be amended.

The most logical device for relieving the co-partners would be an implied agreement by X not to seek repayment (except from partnership profits or assets) for the money he furnished.¹³⁹ Such an argument, as we have already suggested, might be strengthened by the fact that X's co-partners contributed only labor to the partnership. Affirmative proof of the agreement would be required of the co-partners in any event.

Although the general rule of loss sharing in Texas is clear, the "use" and "labor" exceptions are not. Some of the confusion can be laid to the garrulity of the courts in pronouncing needless dicta. The rest is attributable to the "single-shot" character of the early partnership, typical of a farm-and-ranch economy. Land was to be cultivated or livestock fattened; one man furnished the assets, the other the labor. Settlement was made when the crops or cattle were sold; advances and expenses were repaid and the remainder divided as profits. All outlays were, in effect, capitalized as asset costs. There were no liquid funds in the partnership, no concept of the continuous flow of income and expense. There were no periodic reckonings and thus no occasion for interim distribution of profits or contributions to losses.¹⁴⁰ Capital was regarded as an object rather than a measure. Profit was understood as existing apart from assets (*i.e.*, after the assets were disposed of above cost). Loss was understood only as the impairment of an asset capital (*i.e.*, sale below cost), not as a negative profit. Thus the loss was the responsibility of the asset owner, not of the profit sharer. A probable sympathy for the laborer over the capitalist confirmed the result.

Eventually the realization dawned that a loss is the result of an historical process, not of an isolated transaction. This may be sensed in the statement that a loss of capital is to be shared in the same way as if the loss "had . . . not reached the capital, but had simply diminished the profits."¹⁴¹ To complete the present discussion of

¹³⁹ Cf. *Paggi v. Quinn*, 179 S.W.2d 789, 794-95 (Tex. Civ. App. 1944) error ref. w.o.m.

¹⁴⁰ There appear to be no Texas cases dealing with these matters before dissolution. Elsewhere, the common law is that the timing of distributions and contributions is to be decided by majority vote of the partners. *Crane, Partnership* § 65, especially n.11 (2d ed. 1952).

¹⁴¹ *Bivins v. Proctor*, 125 Tex. 137, 152, 80 S.W.2d 307, 314 (1935), quoting from *Bates, Partnership* § 813, at 859 (1888).

losses,¹⁴² it will suffice to note that "capital" is repaid before profits are distributed.¹⁴³ If the capital is impaired (which means there are no profits), whatever capital (*i.e.*, asset capital) exists is shared by the partners not necessarily equally but in proportion to their capital contributions.¹⁴⁴ The partners may, of course, provide otherwise.¹⁴⁵ Regardless of capital impairment, the order of distribution will be the same whether the partnership had the "property" or only the "use" of a particular asset. If it had the "property," the value of the asset increased the contributing partner's capital account and hence his dissolution priority. If it had only the "use," the asset remained his throughout.¹⁴⁶

3. *The Act's Treatment of Profits, Losses, and Capital*

The act codifies the general rules prevailing in Texas but does away with the questionable exceptions. Section 18(a) provides for sharing profits equally and losses in proportion to profits. This specifically applies to losses "whether of capital or otherwise"; the exact nature of "capital" is not in issue since it does not serve as a limitation. The Texas "labor" exception could not arise under the act. The "use" exception might enter via an argument that a loss on disposition of a particular asset was not "sustained by the partnership" since the partnership had only the "use" of the asset. No trace of this exception has been found in cases under the act, and it is unlikely that it would appear in view of the act's broad definition of partnership property.¹⁴⁷ There is no justification in the act for the "use" exception applied to losses unconnected with specific assets.

¹⁴² The order of distribution on dissolution will be treated later in notes 281-82 *infra* and accompanying text.

¹⁴³ But cf. *Bradford v. Bradford*, 172 S.W.2d 365, 367 (Tex. Civ. App. 1943) ("[T]he law will not imply a promise by a co-partner to repay advancements of capital during the continuance or at the dissolution of the partnership.").

¹⁴⁴ *Newman v. Newman*, 145 Tex. 433, 435, 198 S.W.2d 91, 93 (1947), relying on *Johnston v. Ballard*, 83 Tex. 486, 18 S.W. 686 (1892). Cf. *Butler v. Thomasson*, 256 S.W.2d 936, 939 (Tex. Civ. App. 1953) ("[A]s a general rule each partner, upon dissolution . . . is entitled to share in the assets and liabilities in proportion to his investment.").

¹⁴⁵ See *Fromme v. West*, 226 S.W.2d 655 (Tex. Civ. App. 1950) error ref. (jury found contract by F to give W a half interest in crops and cattle in exchange for W's labor; court construed as interest in "profits" but affirmed recovery for W measured by gross value of the assets themselves). See also *Whitis v. Polk*, 36 Tex. 602 (1872) (agreement by P and W to share gross proceeds of cotton furnished by P to be marketed by W implies that they are joint owners of the cotton).

¹⁴⁶ The contrary dictum in *Masterson v. Allen*, 69 S.W.2d 539, 542-43 (Tex. Civ. App. 1934) error ref., must be regarded as invalid.

¹⁴⁷ § 8(1), (2). Cf. *Adams v. Silfen*, 337 Ill. App. 654, 86 N.E.2d 288 (1949) (patents developed by partner D at partnership expense were "partnership asset" not recoverable by D as his contribution to partnership).

The act makes it clear that a partner is entitled to recover his capital contributions and advances before the surplus is shared. This is at variance with some dicta but in accord with the Texas holdings. In particular, under the act, liabilities to partners must be satisfied before capital contributions and advances are repaid. Liabilities would seem to include advances, although this is not clear. Texas law on the point is vague, even failing to distinguish between liabilities and capital contributions.¹⁴⁸

Like the Texas cases, the act is silent as to *when* (other than at dissolution) profits and losses are to be shared.

B. *Indemnity and Contribution*

Texas recognizes the right of a partner to contribution from his co-partners when he pays more than his share of a partnership obligation.¹⁴⁹ The right is based on a promise implied in law.¹⁵⁰ Contribution in this sense is to be distinguished from the contribution a partner may expressly agree to make to partnership capital. It is also to be distinguished, less clearly, from the contribution a partner makes when he shares in partnership losses.¹⁵¹ In the latter case, the economic result will be the same to the extent that the payment contributed to was one which entered into the computation of the loss. The obligation to share losses would not, however, be diminished by making the payments from partnership property, although this would give no contribution right in the sense here used. On the other hand, contribution might be required for a payment which did not increase the loss, *e.g.*, the advantageous purchase of an asset for the partnership.

The best explanation of the contribution right is that a partner who pays more than his share of a partnership obligation becomes a creditor of the partnership for the excess and is thus entitled to collect from it or the co-partners.¹⁵²

The Texas right of contribution corresponds to the right of indemnity under the act.¹⁵³ The word "indemnity" in the act is preferable because it avoids the multiple meanings of "contribution."

¹⁴⁸ Cf. *M. & C. Creditors Corp. v. Pratt*, 172 Misc. 695, 17 N.Y.S.2d 240 (Sup. Ct. 1938), *aff'd*, 255 App. Div. 838, 7 N.Y.S.2d 662 (1st Dep't 1938), *aff'd*, 281 N.Y. 804, 24 N.E.2d 482 (1939) (capital, as distinguished from advances, was intended to be at risk of partnership business).

¹⁴⁹ *Hoxie v. Farmers Bank*, 49 S.W. 637, 639 (Tex. Civ. App. 1899) error ref.

¹⁵⁰ *Ibid.*

¹⁵¹ See note 125 *supra* and accompanying text.

¹⁵² *Paggi v. Quinn*, 179 S.W.2d 789, 794 (Tex. Civ. App. 1944) error ref. *w.o.m.*; *Diamond v. Gust*, 206 S.W. 366, 369 (Tex. Civ. App. 1918) error ref.

¹⁵³ § 18(b).

The act is perhaps broader in covering liabilities incurred as well as payments made, while Texas apparently has considered solely the latter.¹⁵⁴

Texas cases deal with contribution only as of the time of dissolution, although logically the right arises immediately upon payment. Like other rights for money growing out of the partnership relation, it cannot be enforced until the final accounting. The act is silent on the timing of the indemnity right.

The act's inclusion of payments for the preservation of partnership business or property (in addition to payments in the ordinary course of its business) probably represents no extension of Texas law, which has not, however, been explicit on this point.¹⁵⁵

C. Compensation for Services, Money, and Property

A partner's share of the profits is his compensation for services.¹⁵⁶ He is entitled to the profits even though he fails to perform the services promised by him,¹⁵⁷ although he may be liable for damages.¹⁵⁸ Without a specific agreement¹⁵⁹ he is not entitled to any other compensation for his services,¹⁶⁰ even though there are no profits to share¹⁶¹ or he rendered extra services because his co-partners failed to fulfill their service obligations.¹⁶² The reason has been offered that each partner is a principal rather than an employee;¹⁶³ more cogently, it is that one kind of compensation will not be inferred where another (profit sharing) has been expressed.

Several variations from these principles must be noted. An early Supreme Court decision affirmed an arbitration award which in-

¹⁵⁴ *Hoxie v. Farmers Bank*, 49 S.W. 637 (Tex. Civ. App. 1899) error ref. (suggestion that the right arises when the partner pays the judgment against him for a partnership debt, not when the judgment is entered).

¹⁵⁵ Cf. *Moss & Urschel v. Clark*, 82 S.W.2d 1090, 1093 (Tex. Civ. App. 1935) error ref. (contribution for payment "necessary in the development, protection and operation" of the partnership oil and gas lease).

¹⁵⁶ *Montgomery v. Burch*, 11 S.W.2d 545 (Tex. Civ. App. 1928) error dism.

¹⁵⁷ This is the implication of cases like *Wilson v. Hunt*, 270 S.W. 263 (Tex. Civ. App. 1925), holding that the co-partner is not entitled to anything more than his own share of the profits. Cf. *Bauer v. Crow*, 110 Tex. 538, 221 S.W. 936 (1920) (no services called for, profits shared).

¹⁵⁸ *Fithel v. Saltes*, 11 S.W.2d 815 (Tex. Civ. App. 1928) error ref. (absent partner charged with cost of hiring employee to do his job).

¹⁵⁹ For an example of a valid, specific salary agreement, see *Trigg v. Shelton*, 249 S.W. 209 (Tex. Comm. App. 1923).

¹⁶⁰ *Butler v. Thomasson*, 256 S.W.2d 936 (Tex. Civ. App. 1953).

¹⁶¹ *Johnston v. Steele*, 107 S.W. 631 (Tex. Civ. App. 1908).

¹⁶² *Fithel v. Saltes*, 11 S.W.2d 815 (Tex. Civ. App. 1928) error ref. (co-partner absent because of illness); *Wilson v. Hunt*, 270 S.W. 263 (Tex. Civ. App. 1925) (co-partner's failure to perform not explained).

¹⁶³ *Heilbron v. Stubblefield*, 203 S.W.2d 986, 989 (Tex. Civ. App. 1947) error ref. n.r.e.

cluded an allowance to a farming partner for his services. Distinguishing a trade or professional partnership (to which each partner is presumed to devote his time and attention), the Court said:

It [the partnership in question] only embraced the purchase and running of a farm; and if one partner in such case should, at the instance of the other, devote his time and attention to the farm, while the other was devoting his attention to his individual business, we have no doubt but that the law would imply a promise that the former should have compensation for his services.¹⁶⁴

Quite apart from the oblique language and the absence of citation, this decision is weak in logic. The disparity of services (particularly since normal in the business) would naturally have been taken into account in determining the division of profits.¹⁶⁵ Nonetheless, the decision appears still to stand. Its only important application has been in a more compelling situation where a partner was allowed a salary for services expected to be performed by hired help.¹⁶⁶ In both cases the non-labor partner was concerned with his individual affairs and in some way asked or agreed that his co-partner do all the partnership work. In the latter case, however, the need for one partner to do all the work was not anticipated while in the former it was. Therefore, a supplemental, implied contract is justifiable in the more recent case but not in the older one where the original contract (for profit sharing) should have been decisive.¹⁶⁷

One other exception to the general rule allows compensation for services by a partner when his co-partner "abandoned the partnership before its affairs were wound up" and the partner "was forced to render services to the partnership not contemplated by the partnership agreement."¹⁶⁸ To reconcile the exception with the general rule, it must be inferred that abandonment is something more serious

¹⁶⁴ *Hooker v. Williamson*, 60 Tex. 524, 527 (1883). The case is discussed here in some detail since, through the vagaries of head-noting, it has eluded Texas Digest and Texas Jurisprudence. Another early case said a partner could recover the value of his services (constructing a plant to be operated by the partnership) when he was "expelled" from the partnership on completion of the construction. *Ball v. Britton*, 58 Tex. 57 (1882). A dissolution rationale is used: the partner should be able to withdraw the property equivalent of his services contribution.

¹⁶⁵ It may be economically unrealistic to assume that a labor partner has the same bargaining power as an asset partner, but this is implicitly done in ruling that the labor partner shares "capital" losses without an express agreement to the contrary, notes 131-32 *supra* and accompanying text.

¹⁶⁶ *Montgomery v. Burch*, 11 S.W.2d 545 (Tex. Civ. App. 1928) error dism.

¹⁶⁷ It may be argued that, in the latter case, the absence of an employee should have been anticipated just as it is presumed that the absence of a partner should have been anticipated in setting the profit shares. The answer, of course, is that replacement by a partner is natural in a partner's absence but not in an employee's.

¹⁶⁸ *Siler v. Barber*, 29 S.W.2d 829, 831 (Tex. Civ. App. 1930) error dism.

than failure to perform services (which would not justify compensation for the other partner), or that voluntary failure to perform (as distinguished from involuntary) is not contemplated at the formation of the partnership agreement, or that services in winding up are treated differently from services in the continuation of the business (although they are certainly as natural and foreseeable).

The act¹⁶⁹ comports generally with the Texas cases disallowing compensation for a partner's services. It would establish the rule suggested in one case¹⁷⁰ that compensation is allowable to the partner who winds up. Although the act purports to deny remuneration in all other cases, it is subordinate to agreements among the partners. Thus, it would be possible, though not necessarily desirable, to reach the same results under the act as under the Texas decisions on implied agreements.¹⁷¹

It is normally reasoned that profit sharing compensates for the furnishing of capital just as it does for the furnishing of services. Consequently, without an express agreement to the contrary, no interest is due a partner on his capital in the firm.¹⁷² Interest is allowed from the time an accounting is completed and repayment of the capital is due,¹⁷³ but this is for delay in the payment of a matured debt, not for use of the capital in the business. One case allowed interest where there was no express agreement for it but it was found (on unstated criteria) that the capital contributions were in effect loans.¹⁷⁴

The act is perfectly clear: a partner is entitled to interest on his capital only from the date repayment should be made.¹⁷⁵

There is little Texas authority on the right of a partner to receive rent for property he supplies for partnership use. It would seem that his share of profits would be the only compensation owing to him. One case has, however, granted rent based on an implied contract.¹⁷⁶ Nothing in the act purports to deal with this problem.

¹⁶⁹ § 18(f).

¹⁷⁰ *Siler v. Barber*, 29 S.W.2d 829 (Tex. Civ. App. 1930) error dism.

¹⁷¹ *Hooker v. Williamson*, 60 Tex. 524 (1883); *Montgomery v. Burch*, 11 S.W.2d 545 (Tex. Civ. App. 1928) error dism.

¹⁷² *McKay v. Overton*, 65 Tex. 82 (1885); *Jones v. Mitchell*, 47 S.W.2d 371 (Tex. Civ. App. 1932) error ref.

¹⁷³ *Ibid.* Cf. *Corralitos Co. v. MacKay*, 72 S.W. 624 (Tex. Civ. App. 1903) error ref. (interest allowed where accounting delayed by fraud or misconduct).

¹⁷⁴ *Reese v. Carey Bros.*, 286 S.W. 307, 314 (Tex. Civ. App. 1926) error dism. Cf. *Giddings v. Harding*, 267 S.W. 976 (Tex. Comm. App. 1925) (interest paid by partner to third person on sums borrowed by partner to purchase cattle for partnership was allowed as a partnership expense, thereby paid to partner).

¹⁷⁵ § 18(d).

¹⁷⁶ *Meier v. Murphy*, 207 S.W.2d 947 (Tex. Civ. App. 1948) error ref. n.r.e.

The act's chief contribution to the treatment of compensation is to focus attention on the profit-sharing agreement as the primary means of remuneration and to discourage implied supplementary agreements.

D. *Management*

In Texas, each partner has the right to share in the management of the firm affairs.¹⁷⁷ Control normally rests in the majority,¹⁷⁸ but it may be delegated, e.g., to a managing partner.¹⁷⁹ The act is entirely in accord.¹⁸⁰

E. *Delectus Personae*

In the only Texas case¹⁸¹ dealing with the phrase, *delectus personae* has been described as the right of the partners to select their co-partners. In particular, this means that no person can become a member of a partnership without the unanimous consent of the existing partners.¹⁸² It is in this form that the act lays down the rule.¹⁸³

F. *Fiduciary Relations*

Texas cases recognize the fiduciary aspect of partners' relations with one another, growing out of their intimate association, essential dependence, and mutual confidence. They may not deal with each other at arms length, but must voluntarily disclose all information relevant to the partnership,¹⁸⁴ e.g., concerning the value of its property.¹⁸⁵ A partner who acquires property for his own benefit,

¹⁷⁷ *Rische v. Rische*, 101 S.W. 849 (Tex. Civ. App. 1907) error dism. (refusal to allow participation in management is sufficient ground for decree of dissolution and receivership).

¹⁷⁸ *Oil Lease & Royalty Syndicate v. Beeler*, 217 S.W. 1054, 1057 (Tex. Civ. App. 1920) error ref. (dictum).

¹⁷⁹ *Ibid.* Cf. *Texas Unemployment Compensation Comm'n v. Bass*, 137 Tex. 1, 151 S.W.2d 567 (1941) (partnerships with majority partners in common were not "controlled . . . by the same interest" because they had separate managing partners; consequently, they were not to be treated as a single partnership for unemployment compensation purposes). For an example of extensive powers of a managing partner, see *Trigg v. Shelton*, 249 S.W. 209 (Tex. Comm. App. 1923).

¹⁸⁰ § 18(e), (h). Nothing has been found in the Texas cases to correspond to the last clause of § 18(h), but it is entirely consistent with other phases of the Texas law.

¹⁸¹ *Johnston v. Winn*, 105 S.W.2d 398 (Tex. Civ. App. 1937) error dism.

¹⁸² *Ibid.*

¹⁸³ § 18(g).

¹⁸⁴ Cf. *Pappas v. Gounaris*, 301 S.W.2d 249, 253 (Tex. Civ. App. 1957), reformed and aff'd, —Tex.—, 311 S.W.2d 644 (1958) (duty to disclose homestead claim in property contributed to partnership).

¹⁸⁵ *Johnson v. Peckham*, 132 Tex. 148, 120 S.W.2d 786 (1938) (negotiation by partner to sell for higher price than he was paying co-partner for his interest; sale between partners must be for fair consideration and on full disclosure); *Inman v. Parr*, 311 S.W.2d 658, 701-02 (Tex. Civ. App. 1958) (periodic statements of profits and net worth of automobile

adverse to the partnership interests and without his co-partners' consent, holds the property in trust for the partnership.¹⁸⁶ The result is similar if he misappropriates partnership property.¹⁸⁷ Where he withholds property due the partnership, the judiciary has held him liable but not on trust principles.¹⁸⁸ There are decisions to the effect that surviving partners hold money collected upon partnership claims in trust for the partnership, and must account to the deceased partner's representative for his share.¹⁸⁹

In this province, as the Commissioners noted,¹⁹⁰ the act¹⁹¹ does little more than clarify doubt, specifying that a partner holds *as trustee* "any profits" improperly derived by him. By contrast, using no "trustee" language, the act says that a partner *must account for* "any benefit" (as distinguished from "any profits"). It is hard to believe that any lesser standard was intended for something that might represent a benefit but not a profit, *e.g.*, misappropriated partnership property. The solution may lie in a generous definition

dealership); *Rodgers v. Tracy*, 242 S.W.2d 900 (Tex. Civ. App. 1951) error ref. n.r.e. (newly developed geological interest in "deep rights"); *Perpetual Royalty Syndicate v. Albritton*, 149 S.W.2d 700 (Tex. Civ. App. 1941) error dism., judgm. cor. Cf. *Armstrong v. Simms*, 132 S.W. 500, 501 (Tex. Civ. App. 1910), which suggests that there is no affirmative duty to disclose, only a duty not to deceive.

¹⁸⁶ *Wampler v. Harrington*, 261 S.W.2d 883 (Tex. Civ. App. 1953) error dism. What is "adverse" for this purpose remains to be defined by the Texas courts. In this case it appears merely that the lease acquired by one partner individually was of the kind sometimes acquired by the partnership. Cf. *MacDonald v. Follett*, 142 Tex. 616, 180 S.W.2d 334 (1944); the decision is not on partnership grounds, but the adverseness is clear: M individually obtained renewal of an overriding royalty formerly held jointly by him and F. See also *Smith v. Bolin*, 153 Tex. 486, 271 S.W.2d 93 (1954), holding that a managing partner held in trust for the partnership an oil and gas lease on land previously leased to the partnership if he was in fiduciary relationship when he individually obtained the later lease. Although it was found on remand that a fiduciary relationship did exist, 294 S.W.2d 280 (Tex. Civ. App. 1956) error ref. n.r.e., it is not clear what criteria were used. The central issue, quite properly, seems to have been whether the partnership still existed when the new lease was made, but there is a suggestion that the fiduciary relationship is independent of the partnership. Cf. *Collins v. Gee*, 107 S.W.2d 754 (Tex. Civ. App. 1937) error ref., where property owned by G and associates was foreclosed by their agreement with the mortgagee; later G bought the property for substantially less than the mortgage debt. It was held that G had no obligation to share the property with the associates since they had voluntarily parted with it to relieve themselves of the mortgage debt and had completely terminated the association.

¹⁸⁷ *Cook v. Barrier*, 73 S.W.2d 623 (Tex. Civ. App. 1934) (partner used partnership funds for individual speculation in cotton); *Pfeuffer v. Haas*, 55 S.W.2d 111 (Tex. Civ. App. 1932) error dism. (partner allowed employee to use partnership funds to pay employee's debts); *Smith v. Green*, 243 S.W. 1006 (Tex. Civ. App. 1922) error ref. (partner used partnership funds to improve his homestead).

¹⁸⁸ *Collins v. Dawson*, 54 S.W.2d 256 (Tex. Civ. App. 1932) error dism. (commission on stock sale for which partnership was broker).

¹⁸⁹ *Iowa Mfg. Co. v. Baldwin*, 82 S.W.2d 994 (Tex. Civ. App. 1935) error dism.; *Amarillo Nat'l Bank v. Harrell*, 159 S.W. 858 (Tex. Civ. App. 1913) error ref.

¹⁹⁰ Commissioners' Note to § 21.

¹⁹¹ § 21.

of "profit," which the courts of Texas would undoubtedly give in preservation of existing case law applying trust principles.¹⁹²

The act's broad inclusion of "profits . . . connected with the formation, conduct or liquidation" of the partnership, extends trust principles to the "twilight" zones before and after the actual operation of the partnership business.¹⁹³ The statutory trust would enable the partnership to regain intact money or property held by a partner despite insolvency or the statute of limitations. The act also imposes a duty to render information on demand of a co-partner.¹⁹⁴ This is weaker than the Texas duty to render information without demand (e.g., in trading with a co-partner) but the latter would surely persist as a corollary of the fiduciary character of partners under the act.¹⁹⁵

G. Books and Records; Formal Accounts

Texas courts have stated that it is the duty of a managing partner to keep accurate records of his transactions.¹⁹⁶ Apparently, nothing has been said about the record-keeping requirements where there is no managing partner; presumably, each partner should record his partnership transactions or report them to the bookkeeping partner or clerk. The act specifies that the books shall be at the principal place of business;¹⁹⁷ as to record-keeping, it requires only that partners shall render full information on demand.¹⁹⁸ A partner's right to inspect the books is recognized in Texas¹⁹⁹ and the act.²⁰⁰

¹⁹² See note 147 *supra* and accompanying text.

¹⁹³ See, e.g., *White v. McNeil*, 294 S.W. 928 (Tex. Civ. App. 1927), in which M agreed to become W's partner and to convey to him a half interest in certain leases to be used in the partnership. Two days later M advised that he would not perform. W sued for his half interest in the leases. Dismissal on M's general exceptions was affirmed on the ground that the leases had never become partnership property and the agreement to convey was unenforceable since unwritten. Except possibly for the statute of frauds question, the result would be contrary under the act. The act would produce the same result as *McLean, v. Hargrove*, 139 Tex. 236, 162 S.W.2d 954 (1942), holding that a surviving partner, despite his authority to wind up, was a constructive trustee for partnership property which he individually purchased below actual value at a post-dissolution foreclosure sale which he could have prevented.

¹⁹⁴ § 20.

¹⁹⁵ Cf. *Poss v. Gottlieb*, 118 Misc. 318, 193 N.Y.S. 418 (1st Dep't 1922) (partner should abstain from all concealment).

¹⁹⁶ *Saunders v. Duval's Adm'r*, 19 Tex. 467, 472 (1857); *Newman v. Newman*, 195 S.W.2d 393, 397 (Tex. Civ. App. 1946), *aff'd*, 145 Tex. 433, 198 S.W.2d 91 (1946); *Cook v. Peacock*, 154 S.W.2d 688, 690 (Tex. Civ. App. 1941) error ref.; *Dial v. Martin*, 37 S.W.2d 166, 180 (Tex. Civ. App. 1931), *rev'd on other grounds*, 57 S.W.2d 75 (Tex. Comm. App. 1933). Some aspects are effectively determined by federal tax law, e.g., fiscal year and segregation of certain accounts. Int. Rev. Code of 1954, §§ 706, 702.

¹⁹⁷ § 19.

¹⁹⁸ § 20.

¹⁹⁹ *Rush v. Browning*, 103 Tex. 649, 132 S.W. 763 (1910); *Saunders v. Duval's Adm'r*, 19 Tex. 467 (1857).

²⁰⁰ § 19.

A formal account or (as it is sometimes called) an accounting is more than a presentation of financial statements. It encompasses a review of all transactions, including alleged improprieties, which should be reflected in the financial statements.

Texas cases seem to recognize a partner's right to an accounting at dissolution but not before.²⁰¹ If the partnership agreement called for periodic accounting, a Texas court would probably enforce it, but there are no cases in point. The act therefore represents an advance in allowing a partner a formal account where the right to it exists under the terms of any agreements.²⁰² The act is also explicit in granting an accounting to a partner who is wrongfully excluded or whose co-partner violates fiduciary obligations or withholds money.²⁰³ Texas would probably reach the same result in these events by treating them as grounds for dissolution which would be followed by an accounting.²⁰⁴ In these and any other circumstances rendering an accounting "just and reasonable" the act provides it without dissolution.²⁰⁵ The act's procedure should be speedier and less injurious to the partnership whose affairs are incomplete or which is to last for a fixed term.

IV. DISSOLUTION OF A PARTNERSHIP

The Uniform Partnership Act offers major improvements over Texas case law in the treatment of dissolution. The first of these is a clarification of terminology. Texas does not distinguish the time when the partners cease to go forward as full-fledged associates and the end of the wind-up period that follows. Judges have applied "termination" and "dissolution" indiscriminately to both situations, thus failing to differentiate a change in legal status from the completion of an economic activity. The confusion of thought that results from this confusion of language is avoidable under the act, which defines dissolution as the change in relations caused by any partner ceasing to be associated in the carrying on of the business, as distinct from its winding up.²⁰⁶ The act specifies that a partner-

²⁰¹ See, e.g., the language in *Miller v. Howell*, 234 S.W.2d 925 (Tex. Civ. App. 1950), at 930: "When a partnership business is closed out, a cause of action for an accounting arises between the partners . . ."

²⁰² § 22(b). Failure to furnish such an account may be grounds for dissolution under § 32(1)(d).

²⁰³ § 22(a), (c).

²⁰⁴ Such events would also be causes of dissolution under the act. *Herslof v. Sharpe*, 249 Wis. 600, 24 N.W.2d 600 (1946).

²⁰⁵ § 22(a), (c), (d). *Morris v. Duke*, 175 Md. 300, 2 A.2d 11 (1938).

²⁰⁶ § 29.

ship continues after dissolution until the winding up is completed.²⁰⁷ Then it terminates.²⁰⁸

These rules of the act greatly simplify solution of such questions as who shares in post-dissolution profits or which partners may be held liable on obligations incurred after dissolution.

*A. Causes of Dissolution*²⁰⁹

A partnership is a fragile thing; its essential community of interests is easily destroyed. Dissolution may happen in a variety of ways. For example, both the act and Texas decisions recognize that death of a partner²¹⁰ and absence of profit prospect²¹¹ dissolve the partnership or justify dissolution.

Other causes of dissolution in the act appear to be consonant with Texas principles but have no exact parallel in the cases. These include completion of the term or undertaking specified in the partnership agreement,²¹² supervening illegality or (upon judicial determination under the act) lunacy or other incapacity,²¹³ and bankruptcy or insolvency.²¹⁴

²⁰⁷ § 30.

²⁰⁸ Commissioners' Note to § 29.

²⁰⁹ Until recently, a vexatious question was what constituted dissolution or termination for federal income tax purposes, especially with respect to death of a partner or sale of a partnership interest. See Jackson et al., *The Internal Revenue Code of 1954: Partnerships*, 54 Colum. L. Rev. 1183, 1196 (1954). The tax law now provides that a partnership continues unless no part of its business is carried on in a partnership or a 50% interest changes hands within a year. Int. Rev. Code of 1954, § 708.

²¹⁰ § 31(4). *Martin v. Dial*, 57 S.W.2d 75 (Tex. Comm. App. 1933). It should be noted that Texas dicta indicate that a partnership may continue despite the death of a partner, if there is a specific agreement to this effect. *Alexander's Ex'rs v. Lewis*, 47 Tex. 481 (1877). See Comment, *Partnership Agreement Disposing of Property After Death*, 7 Baylor L. Rev. 291 (1955). This case, and most subsequent authorities, express doubt whether there is technically a continuation of the old partnership in these circumstances, or the formation of a new one. The act provides for a clear continuation of creditors' rights in such circumstances. § 41.

²¹¹ Section 32(1)(e) requires a court determination. *Collins v. Lewis*, 283 S.W.2d 258 (Tex. Civ. App. 1955) error ref. n.r.e. (dictum; case holds that plaintiff partner cannot obtain dissolution on this ground where jury has found that profits are possible but for his interference).

²¹² § 31(1)(a). Cf. *Trigg v. Shelton*, 249 S.W. 209 (Tex. Comm. App. 1923) (agreement validly gave one partner the right to dissolve at any time). Section 23 provides that a continuation of the partnership business by the active partners after completion of the specified term or undertaking creates a partnership at will otherwise subject to the original agreement.

²¹³ § 32(3). Cf. *King v. Matney*, 259 S.W.2d 606 (Tex. Civ. App. 1953) error ref. n.r.e. (marriage of female partner dissolves).

²¹⁴ §§ 31(5), 2. These provisions cover bankruptcy (i.e., adjudication under National Bankruptcy Act §§ 1(2) and 1(8)) of the partnership or of any partner. Texas law has not reached this degree of refinement; the only discovered case states that bankruptcy of a partner dissolves the partnership. *Daugherty v. Jacob Strauss & Co.*, 1 White & Willson 508 (Tex. Comm'rs of App. 1880). The same sections of the Uniform Partnership Act provide dissolution when the partnership or any partner is insolvent under a state insolvency act.

Still other causes of dissolution included in the act must be regarded as potential modifications of Texas law since there is insufficient background to predict how a Texas court would rule: expulsion of a partner pursuant to a power contained in the partnership agreement,²¹⁵ or a judicial determination that a partner has wilfully or persistently breached the partnership agreement or that his conduct tends "to affect prejudicially" or makes "not reasonably practicable" the carrying on of the partnership business.²¹⁶

Under Texas law, a partner's sale of his interest in the partnership or in partnership property effects a dissolution.²¹⁷ As already discussed, the act would make a welcome change by ruling that such a transfer does not, in itself, bring about dissolution.²¹⁸ The transferee could dissolve if the partnership had completed its term or undertaking, or was a partnership at will,²¹⁹ but could not other-

The general Texas test of insolvency is the equity test: inability to pay debts as they mature. 24A Tex. Jur., Insolvency §30 n.9 (1956) and cases there cited. But Texas has no insolvency statute in force. Nor is it even clear in Texas law how the insolvency test would be applied to a partnership, that is, whether only partnership ability to pay debts would be considered, or whether the partners' individual abilities to pay partnership debts would be taken into account in consequence of their unlimited liabilities. The latter would probably be the Texas ruling, since it is consistent with the local interpretation of a partnership as a contractual aggregation of individuals rather than a separate legal entity. Nonetheless, one can not say with certainty that a Texas partnership could be insolvent while it still had a solvent member.

This doubt is one of several factors encouraging the use of federal bankruptcy procedures in the disposition of Texas partnerships. By federal standards, insolvency is measured from the balance sheet by determining whether the debts exceed the assets at a fair value. Assets of a partnership include the excess, if any, of each partner's individual assets over his individual debts. (Cases are collected in 1 Collier, Bankruptcy 698-99, Para. 5.06 nn.1-4 (14th ed. 1956, Supp. 1957)). Conversely, in determining whether an individual partner is insolvent, his assets are deemed to include his share of the partnership assets in excess of partnership debts. Thus, entity principles are applied to the extent of preserving the priority of individual creditors in individual assets and of partnership creditors in partnership assets. But aggregate principles are applied secondarily so that a partnership will never be insolvent for bankruptcy purposes if it has a solvent partner.

The Uniform Partnership Act resembles the bankruptcy law in counting as partnership assets the contributions which partners are required to make in order to satisfy partnership liabilities. § 40(a) (II).

Determining, under the bankruptcy act, that a partner or partnership is bankrupt involves many complications into which we cannot enter here. Primary among these is what constitutes an act of bankruptcy by a partnership, especially in respect of a fraudulent or preferential transfer. See 1 Collier, Bankruptcy 696-98 (14th ed. 1956); Crane, Partnership § 91 (2d ed. 1952).

²¹⁵ § 31(1)(d). The novelty is that the act specifies that such a dissolution is not in violation of the agreement, an entirely reasonable view. The only remotely relevant authority seems to be *Rische v. Rische*, 101 S.W. 849 (Tex. Civ. App. 1909) error dismissed, in which a receivership was granted at the instance of a partner who had been excluded from the partnership; the exclusion was not pursuant to any agreement.

²¹⁶ § 32(1)(c), (d).

²¹⁷ Note 55 *supra* and accompanying text. Cf. *Neal v. Adkins*, 145 S.W. 264 (Tex. Civ. App. 1912) (admission of new partner creates new partnership).

²¹⁸ § 27(1). See discussion in notes 66, 56-57 *supra* and accompanying text.

²¹⁹ § 32(2).

wise interfere or participate in the partnership.²²⁰ The remaining partners could obtain a dissolution decree if their co-partner's transfer constituted a wilful breach of the partnership agreement.²²¹

The act affords flexibility and preserves local custom by providing for dissolution, on court decree, when any circumstances render a dissolution equitable.²²²

Probably the most frequently litigated type of dissolution is one which differs moderately in Texas and the act: dissolution at the will of a partner. There is no doubt, of course, that all the partners together may dissolve.²²³ The situation is less clear if fewer than all want to dissolve.

Texas is committed to the general principle that there are no indissoluble partnerships; consequently, any partner can dissolve at any time.²²⁴ Several limitations on this principle should be mentioned although, as typical Texas dicta, they may be more apparent than real. The rule has been enunciated for partnerships "calling for the personal services of the partners."²²⁵ The implication is that it does not hold for other kinds of partnerships, although nothing has been found explicitly so stating. Indeed, such a qualification would not be easy to defend logically; quite apart from the difficulty of identifying "personal services," there seems no compelling reason to keep partners together against the wish of one of them merely because their tie is one of money rather than labor. Another possible stricture on the general rule is the statement that dissolution at will is available provided it would not injure or defraud the co-partners.²²⁶ The short answer to this thought is that protection against wrongful dissolution can be had by means other than specific performance, *e.g.*, damages or constructive trust.

Yet other exceptions are stated or suggested in the jurisprudence.

²²⁰ § 27(1).

²²¹ § 32(1)(d).

²²² § 32(1)(f).

²²³ Cf. *Brammer v. Wilder*, 122 Tex. 247, 57 S.W.2d 571 (1933). This case also stands for the proposition that dissolution requires more than expression of intent, *i.e.*, a cessation of business activity. Assets were retained and extensive enterprises conducted; the Court said "the facts . . . show as a matter of law that the partnership . . . had not been dissolved." *Id.* at 253, 57 S.W.2d at 573. The act, slightly more flexible, allows dissolution by all partners who have not transferred their interests or had them subjected to a charging order. § 31(1)(c).

²²⁴ *McCollum v. McCollum*, 67 S.W.2d 1055 (Tex. Civ. App. 1934) (partnership will not be continued by injunction).

²²⁵ *Id.* at 1056.

²²⁶ *Green v. Waco State Bank*, 78 Tex. 2, 214 S.W. 252 (1890) (dictum), paraphrased in 32 Tex. Jur., Partnership 491 (1934); *Gilver v. Graham*, 52 S.W.2d 263 (Tex. Comm. App. 1932) (possible holding, using the language of termination rather than dissolution).

The partnership agreement may "foreclose the right . . . to demand dissolution."²²⁷ A partnership without a fixed term may be dissolved at the will of any partner;²²⁸ the implication is that a partnership with a fixed term cannot be so dissolved.

The rationale underlying most of these ideas is a simple one familiar in other areas but not articulated in Texas partnership decisions until comparatively recently. It is that the *right* to dissolve differs from the *power* to dissolve. The limitations, whether contractual or equitable, are upon the right, not the power. The distinction is by no means academic, since dissolution without right may bring various consequences, notably damages for breach of contract.²²⁹ The situation is not, however, quite as simple as the power-right dichotomy suggests. A partner who wants out wants his share of partnership property. This necessitates an accounting. Particularly since accounting is historically an equitable proceeding, he may be met with equitable defenses, e.g., "clean hands," which tend to hamper the exercise of his power to dissolve. The quandary is illustrated in a recent case, *Collins v. Lewis*.²³⁰

Collins, the financing partner in a large cafeteria venture, sued for dissolution, apparently on the principal ground that there was no reasonable expectation of profit. Although the jury found that there was no such expectation, and although this is normally a valid reason for dissolution, the trial court held and the appellate court affirmed that Collins was not entitled to a dissolution decree. The judgment seems to have rested primarily on a further jury finding that, but for Collins' interference in the cafeteria management (from which he was barred by his agreement with Lewis), there was a reasonable expectation of profit. Just what the jury deemed to be interference is not stated in the opinion. Presumably it was Collins' threat and refusal to furnish additional funds for what he claimed were operating expenses (which he was not obligated to provide) but which the court found to be equipping costs (which he was obligated to provide). Other behavior of Collins might well have been considered interference, even though it pertained to the

²²⁷ *Shelton v. Trigg*, 226 S.W. 761, 780 (Tex. Civ. App. 1920), rev'd on other grounds, 249 S.W. 209 (Tex. Comm. App. 1923).

²²⁸ *Wright v. Ross*, 70 S.W. 234 (Tex. Civ. App. 1902) error dism.; *Ware v. Chatham*, 56 S.W.2d 229 (Tex. Civ. App. 1932) error dism.

²²⁹ *Collins v. Lewis*, 283 S.W.2d 258, 263 (Tex. Civ. App. 1955) error ref. n.r.e.; *McCollum v. McCollum*, 67 S.W.2d 1055 (Tex. Civ. App. 1934). Cf. *Butler v. Thomas*, 256 S.W.2d 936, 939 (Tex. Civ. App. 1953) (dissolution "without penalty" possible at any time unless there is contract to the contrary).

²³⁰ 283 S.W.2d 258 (Tex. Civ. App. 1955) error ref. n.r.e.

financial arrangements rather than the daily operation of the cafeteria. For example, he caused a bank (of which he was a stockholder and director) to mature large demand notes, given by Lewis as part of the transaction but on the understanding from Collins that the only required payments would be from cafeteria earnings at a minimum rate guaranteed by Lewis. Collins then attempted to foreclose the mortgage Lewis had given him on his share of the partnership. Thus, Collins and Lewis, now implacable adversaries, are left in business together although Collins has manifested in the most emphatic way his desire to get out. The result is undoubtedly fair in view of Collins' harrassment of Lewis and in view of the contemplated duration of the project in which profit sharing was to begin only after profits had been applied to discharge installation loans which ultimately exceeded \$600,000. It appears that Collins was asking dissolution as of right (*i.e.*, without liability);²³¹ this was correctly denied him since no person should have a right growing out of his own wrong. The court carefully remarks that the power of dissolution exists apart from this litigation and mentions (conspicuously not adopting it) Collins' contention that the right of dissolution is independent of who is right or wrong in the dispute between the partners. Nonetheless, the reader of the decision is bound to wonder whether the court would have countenanced the *power* of dissolution in the same circumstances in which it was denying the *right*. If the legal right "rests on equity,"²³² so must the exercise of the power. The court's reasoning suits the two situations equally well.

Collins v. Lewis contains this indisputable observation: "The proper and equitable solution of the differences which arise between partners is never an easy problem, especially where the relationship is as involved as this present one."²³³

²³¹ The pleadings are not discussed at any length; the court plainly regards them as seeking dissolution of right. Apparently there was no claim that the partnership was one at will; this would have been incompatible with the long-term undertaking. The court, if it saw fit, could have treated the partnership as dissolved by the act of filing the suit. Cf. *Wright v. Ross*, 70 S.W. 234 (Tex. Civ. App. 1902) error dism. Certainly on the basis of Collins' acts, Lewis could have obtained a decree of dissolution and damages (for which he asked in the event Collins was granted dissolution). Note that it is the service partner (Lewis) asking continuation of the firm; if he were requesting dissolution, he might invoke the argument that his services should not be compelled by prolongation of the partnership. There is no good reason why this theory should be used by him more effectively than against him, for this case dramatically demonstrates the folly of assuming that a non-service relationship is an impersonal one that can be specifically enforced without disruption of the enterprise.

²³² 283 S.W.2d at 261.

²³³ 283 S.W.2d at 263.

The value of the partnership enterprise lay not merely in its property but in its continued operation; this required the capital of Collins and the services of Lewis. The cafeteria could not very well have been partitioned between them, nor is it likely that it could readily have been sold at a satisfactory price. The court, conscious of the difficulty of fashioning a remedy, decided that none was needed because there had been no dissolution. One may agree with the result without accepting the logic. The case remains a bulwark against abuse of the right to dissolve, a threat to the power to dissolve, and a testimonial to the fine line between right and power.

The Texas distinction between the power and the right to dissolve is comparable to the act's distinction between dissolution with and without violation of the partnership agreement.²³⁴ If a definite term or particular undertaking is specified by the partnership agreement, the express will of any partner can dissolve the partnership, but only in violation of the agreement (the consequences of which, far more precise than anything in Texas law, are discussed below). If there is no definite term or particular undertaking, the express will of a partner dissolves without violation.

B. Consequences of Dissolution

1. Relations Among the Partners

Texas law is full of gaps in the subject of partners' relations after dissolution.²³⁵ One of the greatest attractions of the act is its comprehensiveness in this regard. What there is of Texas law has evolved in cases of dissolution by death. Of these, *Martin v. Dial*²³⁶ is authority for all the basic propositions. The surviving partner

²³⁴ § 31(2), (1)(b).

²³⁵ On the whole, Texas courts have failed to distinguish solvent from insolvent dissolutions in terms of either the powers to wind up or the method of distribution. For this and other reasons, most reported instances of the administration of insolvent partnerships are under the federal bankruptcy laws. The latter topic, beyond the scope of our Article, is exhaustively treated in 1 Collier, Bankruptcy 712-43 (14th ed. 1956). See also Crane, Partnership §§ 92-95 (2d ed. 1952). For present purposes, it is sufficient to note that bankruptcy administration supersedes state and private proceedings and gives a trustee, rather than the partners, the right to wind up. Moreover, it controls the distribution of property in such a way as generally to preserve the priority of partnership creditors in partnership assets, and the priority of individual creditors of a partner in his individual assets. These distribution rules are essentially the same as those in the Uniform Partnership Act. § 40(b), (i).

²³⁶ 57 S.W.2d 75 (Tex. Comm. App. 1933). The case is not as strong as it might be since it is not a contest between the survivor and his deceased co-partner's representative but a cooperation between them against one to whom they transferred property which later greatly increased in value. Other sources of copious dicta on the consequences of dissolution are *Smith v. Wayman*, 148 Tex. 318, 224 S.W.2d 211 (1949); *McLean v. Hargrove*, 139 Tex. 236, 162 S.W.2d 954 (1942).

has the duty and authority to wind up the partnership affairs.²³⁷ For this purpose he takes equitable title to partnership property,²³⁸ is entitled to exclusive possession of it,²³⁹ and has the right to sell it (which, importantly, includes the right to execute oil and gas leases of it). He may renew debts²⁴⁰ or mortgage property to pay them. And he may bind the estate of the deceased partner to the extent appropriate and necessary to settle affairs of the firm. His authority does not lapse with the passage of time, though he may be compelled to hasten when he is dilatory. All of the foregoing principles appear to be predicated on the existence of partnership debts,²⁴¹ although there is no indication whether the debts must be substantial in relation to the value of the partnership, and no certainty what happens when the debts are discharged.²⁴²

If the dissolution is by unanimous agreement, each partner can engage in the winding up; he remains an agent of his co-partners for this limited activity. Although he has no authority to undertake new business for the firm, he is entitled to contribution for his reasonable expenses in protecting partnership property.²⁴³

Will these rules apply in other situations? Do we treat an insolvent or rightfully dissolving partner as though he were dead? Is a wrongfully dissolving partner permitted to participate in the winding up? Questions of this sort cannot be firmly answered in the present state of affairs.

The act presents systematic, if somewhat involved, answers to these and other questions arising in dissolution. The right to wind up is (subject to any agreement the partners may have made)

²³⁷ Accord, *Wright v. Campbell*, 75 Tex. 644, 13 S.W. 293 (1890) (surviving law partners may recover from client for services of deceased partner); *McLean v. Hargrove*, supra note 236. The partners may by agreement provide for winding up by persons other than partners, e.g., designated trustees. *Smith v. Wayman*, supra note 236.

²³⁸ See also discussion in notes 46, 63, 67 supra, and accompanying text.

²³⁹ Cf. *Lawrence v. Lawrence*, 156 S.W.2d 559 (Tex. Civ. App. 1941) (receiver will not be appointed to take partnership property from surviving partner unless shown necessary for preservation of the property). The partners may by agreement provide that title shall vest in one of them individually, e.g., in consideration for his assumption of debts. *Gaut v. Reed Bros. & Co.*, 24 Tex. 46 (1859).

²⁴⁰ Contra, *White v. Tudor*, 24 Tex. 639 (1860).

²⁴¹ Cf. *Donnell v. Talley*, 104 S.W.2d 920 (Tex. Civ. App. 1937) error dism. by agr. (surviving partner not entitled to exclusive possession if no debts).

²⁴² Compare *Donnell v. Talley*, supra note 241 (if no debts, partners are tenants in common) with *Newman v. Newman*, 195 S.W.2d 393 (Tex. Civ. App. 1946), aff'd, 145 Tex. 433, 198 S.W.2d 91 (1947) (partnership property not susceptible of partition in kind should be sold and the proceeds divided).

²⁴³ *Jones v. Mitchell*, 47 S.W.2d 371 (Tex. Civ. App. 1932) error ref. (one of three voluntary assessments paid on bank stock found to be reasonable, hence giving rise to contribution right), discussed note 233 infra. See also *Long v. Garnett*, 59 Tex. 229, 232 (1883).

lodged in the partners who have not wrongfully dissolved.²⁴⁴ The malefactor is thus deprived of any right to interfere further in partnership affairs, but one who dissolves a partnership at will is allowed to participate in the settlement of affairs. Moreover, any partner can, upon cause shown, obtain winding up by the court. This should provide judicial assistance more liberally than it has been available under the Texas receivership provisions which have been sparingly applied to partnerships.²⁴⁵ The right to possession of

²⁴⁴ § 37.

²⁴⁵ In a dispute among partners, control of partnership property is almost always an issue. Often receivership is sought. Article 2293, Tex. Rev. Civ. Stat. Ann. (1950), provides that "Receivers may be appointed . . . in the following cases: 1. . . . [B]etween partners jointly owning or interested in any property or fund, on the application of the plaintiff or any party whose right to or interest in the property or fund or the proceeds thereof is probable, and where it is shown that the property or fund is in danger of being lost, removed or materially injured."

This somewhat confused provision has been construed by the Texas courts in few cases, with apparently only three sustaining the trial court's appointment of a receiver of partnership assets upon a partner's petition. These cases are *Hitt v. Morris*, 250 S.W.2d 408 (Tex. Civ. App. 1952); *Alexander v. Alexander*, 99 S.W.2d 1062 (Tex. Civ. App. 1936); *Holder v. Shelby*, 118 S.W. 590 (Tex. Civ. App. 1909). There have been several cases concerning receiverships of joint interests in partition suits. See *Silva v. C. J. Webster Oil & Gas Co.*, 113 S.W.2d 960 (Tex. Civ. App. 1938) (court refused to appoint a receiver); *Annot.*, 23 A.L.R.2d 583 (1952). To justify a receivership, the applicant must first show that his interest in the property is probable, i.e., he must make out at least a *prima facie* case of joint ownership. *Lawrence v. Lawrence*, 156 S.W.2d 559 (Tex. Civ. App. 1941). After establishing this, he must then sustain the difficult burden of proving that his interest in the property is in danger of being lost because of neglect or mismanagement of the business by its manager, or because of the manager's unfitness. *Ibid.* See also *Rogers v. Rogers*, 150 S.W.2d 139 (Tex. Civ. App. 1941). The case of *Silva v. C. J. Webster Oil & Gas Co.*, *supra*, which involved a joint mineral interest but which was decided under the same provision of article 2293, held that a mere allegation that personal property "might be lost or damaged" (statutory language) is insufficient to justify appointment of a receiver. The plaintiff apparently must allege mismanagement, neglect, or similar deficiencies despite the language of this article. Due to the fact that a receivership of a going business is a drastic remedy, the courts are reluctant to appoint a receiver except in extreme cases; particularly is this true in *ex parte* suits under article 2293, where an applicant will be denied relief except in emergencies of a nature which would cause material injury to plaintiff if the delay necessary for notice were taken. *Head v. Roberts*, 291 S.W.2d 483 (Tex. Civ. App. 1956); *Morris v. Ruegg*, 140 S.W.2d 301 (Tex. Civ. App. 1940).

The only provision of the act in which a receivership is authorized is found in § 28(1) which allows a judgment creditor of a partner to apply to the court which rendered the judgment for a charging order, after which the same court may appoint a receiver of the debtor partner's share of the profits and other money due him from the partnership, or order a sale of the interest charged. It is important to note that this remedy is available only to a judgment creditor of a partner and apparently only upon the perfection of a lien, *cf. Waples-Platter Co. v. Mitchell*, 35 S.W. 200 (Tex. Civ. App. 1895), and not to a partner seeking to protect his interest in dissolution or winding up. However, the act has been construed by the courts of jurisdictions in which it is in force not to preclude receiverships of partnership assets in suits for dissolution under § 32. See, e.g., *Galich v. Brkich*, 103 Cal. App. 2d 187, 229 P.2d 89 (1951); *Dolenga v. Lipka*, 224 Mich. 276, 195 N.W. 90 (1923); *Heisler v. Heisler*, 85 N.Y.S.2d 342 (1948). In view of § 32 and its construction by the courts of other states, Texas' adoption of the act would apparently only supplement our present law so far as receiverships are concerned. The act's provision resembles the right recently given to Texas corporations to have their liquidations carried out under court supervision. Tex. Bus. Corp. Act arts. 6.06A(3), 7.06, 7.07 (1955).

partnership property is at all times in the partners and limited to partnership purposes.²⁴⁶ A deceased partner's rights in firm property vest in the surviving partners.²⁴⁷ Thus the remaining partners' rights to control property and settle affairs are independent of the existence of the debts, which have acquired an exaggerated importance in Texas. The precise incidents of the right to wind up are not detailed in the act, but there is nothing to suggest any constriction of those already recognized in Texas cases. Indeed, the emphasis on cash payment of surplus to partners²⁴⁸ implies wide authority to convert other assets into money. On the other hand, the act does not obstruct buy-and-sell agreements or other contractual variances from the statutory pattern of winding up.²⁴⁹

A major innovation which the act would bring to Texas is an option given the remaining partners to buy out a wrongfully dissolving partner instead of winding up and terminating. The partners who have not wrongfully dissolved may (subject to certain conditions, *e.g.*, unanimity among them) continue the business in the same name and possess the partnership property by paying or securing to the wrongfully dissolving partner the value of his interest at dissolution. Against this they may offset any damages to which they are entitled for his breach of agreement.²⁵⁰ The usefulness of such a provision will depend on economic factors which the law cannot hope to control, such as the ability of the remaining partners to raise funds or obtain a bond.²⁵¹

Some kinds of dissolution under the act (*e.g.*, by supervening illegality or court decree) terminate at once the authority of partners to act for one another except as necessary to wind up affairs or complete pending transactions.²⁵² A partner who proceeds beyond these bounds, regardless of his awareness of the fact of dissolution,

²⁴⁶ §§ 8, 25(2)(a).

²⁴⁷ § 25(2)(d).

²⁴⁸ § 38(1).

²⁴⁹ Cf. *In re Ilg's Estate*, 348 Ill. App. 545, 109 N.E.2d 362 (1952).

²⁵⁰ § 38(2)(b). The partner is entitled to release from partnership liabilities. Good will is not considered in valuing his interest. § 38(2)(c)(II). He may be entitled to interest on the sum owed him or a share of profits. § 42. Both sections are construed and applied in *Vangel v. Vangel*, 45 Cal. App. 2d 804, 291 P.2d 25 (1955).

²⁵¹ Consider the case of *Collins v. Lewis*, 283 S.W.2d 258 (Tex. Civ. App. 1955) error ref. n.r.e., discussed notes 230-34 *supra* and accompanying text. If Lewis sought to force Collins out on the theory that the latter had wrongfully dissolved, Lewis would have either to find money to pay Collins off (which he had already tried and failed to do) or to obtain a bond (which might well be unavailable or prohibitively costly). In either event, he would have to deal with the bank which was a substantial lender through Collins to the partnership and which (particularly in view of Collins' close connection with it) might refuse to permit transfer of its obligation.

²⁵² § 33(1).

cannot obtain contribution from his co-partners for his commitments. However, a partner unaware of less notorious types of dissolution is protected. If dissolution is by a co-partner's act (e.g., expressing his will, rightfully or wrongfully), the partner may have contribution for the liabilities he creates until he has knowledge of the act.²⁵³ And if dissolution is by a co-partner's death or bankruptcy, the partner may have contribution for the liabilities he creates until he has knowledge or notice of these facts.²⁵⁴

2. Relations with Third Parties²⁵⁵

Dissolution effects no change in a partner's liability for existing partnership obligations.²⁵⁶ Novation may operate to relieve the partner if there are appropriate dealings between the creditor and the successor to the partnership.²⁵⁷ These rules are also found in the act which is slightly more explicit as to novation,²⁵⁸ and considerably more detailed as to the rights of creditors when the partnership is continued or reformed after a change in membership.²⁵⁹

A single Texas case²⁶⁰ is the source of most of the Texas law on third parties' rights growing out of post-dissolution transactions with a partner. There is no problem, of course, if the transaction is within the winding up authority of the partner who makes it;

²⁵³ § 34(a). Knowledge is defined by § 3(1) in terms of actual knowledge or knowledge of such other facts as in the circumstances shows bad faith. *Jones v. Mitchell*, 47 S.W.2d 371 (Tex. Civ. App. 1932) error ref., may be in conflict with the act. There was full awareness of dissolution at the time the assessments were paid. The result of the case could be reached under the act only via § 33, i.e., holding that the assessment was necessary to the winding up or to the completion of an unfinished transaction. Either theory is doubtful. An alternative might be the argument that the partnership had not really been dissolved inasmuch as the assessments and perhaps other activities continued more than two years after the agreed dissolution date. Cf. *Brammer v. Wilder*, 122 Tex. 247, 57 S.W.2d 571 (1933).

²⁵⁴ § 34(b). Notice is defined by § 3(2) in terms of spoken or written statements of the facts in question.

²⁵⁵ See also note 235 supra.

²⁵⁶ *Shaw v. Green*, 128 Tex. 596, 99 S.W.2d 889 (1937) (assessment on bank stock owned by partnership before dissolution); *Reed v. Shaw*, 274 S.W. 274 (Tex. Civ. App. 1925) (partnership note).

²⁵⁷ *Commercial Nat'l Bank v. Poulous*, 8 S.W.2d 222 (Tex. Civ. App. 1928) (jury found creditor intended to release old partners when, knowing of dissolution, he accepted renewal note from new partners).

²⁵⁸ § 36.

²⁵⁹ § 41. See notes 91-94 supra and accompanying text.

²⁶⁰ *Thompson v. Harmon*, 207 S.W. 909 (Tex. Comm. App. 1919). See also *Hunt Oil Co. v. Killion*, 299 S.W.2d 316 (Tex. Civ. App. 1957) error ref. n.r.e., holding a partner not liable for obligations incurred in the partnership name after he sold his interest. Apparently he gave adequate notice; in any event, the plaintiffs admitted they had knowledge or notice of the sale. Also interesting is the alternate holding of the same case: a surety is not liable (on its bond issued to the partnership prior to the sale) for any debts incurred after the sale; the bond covered only debts of the partnership which was dissolved by the sale. The surety would be liable only because of estoppel against itself. Estoppel against the ex-partner would make him liable, but not the firm, hence not the surety.

in this event all partners are bound. In other cases, third parties are divided into three classes according to their pre-dissolution relations with the partnership, and their rights are defined as follows in terms of the notice of dissolution they are entitled to receive:

(1) Persons who actually dealt with the partnership before dissolution are entitled to actual notice of dissolution. If it is not given to them, they may hold all the partners liable for post-dissolution transactions of any one of the partners. In all events, of course, they may enforce pre-dissolution obligations against any of the partners.

(2) Persons who did not deal with the partnership before dissolution but had knowledge (actual, not just by general reputation) of its existence are entitled to constructive notice (*i.e.*, by publication) of dissolution. If it is not given them, they may hold all the partners liable for post-dissolution transactions with any one of the partners.

(3) Persons with no pre-dissolution dealings or knowledge are not entitled to any notice. They may recover only against the partner with whom they had post-dissolution transactions.

It will be recognized that estoppel is the principle underlying the Texas rules. It also underlies the provisions of the act which are more elaborate and vary somewhat with the type of dissolution. The act speaks in terms of binding the partnership (*i.e.*, every partner) after dissolution. In general, of course, winding up transactions are binding because they are authorized,²⁶¹ and one who holds himself out as a partner after dissolution is as liable as if no dissolution had occurred.²⁶² The partnership cannot be bound at all if the dissolution is by supervening illegality or bankruptcy of a partner.²⁶³ In these circumstances no one is entitled to notice, regardless of prior relations with the partnership. If dissolution is for any other reason, the results may be classified according to the pre-dissolution relations of the third persons with the partnership.²⁶⁴ This classification is as follows:

(1) Persons who lent pre-dissolution credit to the partnership are entitled to knowledge or notice of the dissolution.²⁶⁵ If it is not given to them, they may hold all the partners liable for post-dissolu-

²⁶¹ § 35(1)(a). But see § 35(3).

²⁶² §§ 35(4), 16.

²⁶³ § 35(3)(a), (b).

²⁶⁴ This is not the primary criterion in the act, which classifies first by type of transaction. The arrangement used here is to facilitate comparison with Texas law. As in any paraphrase of a highly organized statute, there is some loss of precision.

²⁶⁵ Knowledge and notice are specially defined in § 3.

tion transactions of any one of the partners.²⁶⁶ This differs from Texas essentially only in narrowing the protected class of third persons from those with prior dealings to those who have previously lent credit. This eliminates the notice requirement for cash customers and suppliers whose names would probably not appear on the partnership records, and who could therefore not be easily notified.²⁶⁷ The same result is obtained under the act if the partner is acting without authority (*e.g.*, because he has wrongfully dissolved) and the third person has no knowledge or notice of the lack of authority.²⁶⁸ This makes it advisable for the notice of dissolution to state which, if any, of the partners are without authority to wind up.

(2) Persons who did not lend pre-dissolution credit to the partnership but knew of the partnership before its dissolution are entitled to notice by publication.²⁶⁹ This result also harmonizes with Texas law. The act specifically states what the Texas courts would undoubtedly hold if faced with the problem: that, despite failure to give notice, a partner is not bound to one who actually knows of dissolution.²⁷⁰ An analogous result will be had if the partner is acting without authority and the third person has no knowledge or notice of the lack of authority and the same has not been published.²⁷¹ Thus, the published notice of dissolution, like the actual notice to prior creditors, should identify any partners not authorized to participate in the winding up.

(3) Other third persons are not entitled to any notice. Texas is in accord.

3. *Distribution of Assets*

The most difficult and complex problems of dissolution are those attendant on the distribution of assets. At issue are the relations of partners to each other and to their creditors. Specifically, these questions must be answered: what are the assets of the partnership; what priorities are to be observed; are contributions from the partners to pay liabilities necessary, and in what amounts; who may enforce the right to contributions, and what property may be levied upon. Section 40 of the act offers a precise

²⁶⁶ § 35(1)(b)(I). Section 35(2) limits the liability of inactive and unknown partners in this situation.

²⁶⁷ Commissioners' Note to § 35.

²⁶⁸ § 35(3)(c)(I).

²⁶⁹ § 35(1)(b)(II). This contains details of the method of publication. Section 35(2), limiting the liability of an inactive partner, is applicable here, too.

²⁷⁰ *Ibid.*

²⁷¹ § 35(3)(c)(II).

formulation of workable rules which would solve many of the problems left unsolved by the Texas cases.²⁷² Texas courts have too often confused the law by their generous use of equity principles.

Section 40 has nine subsections, which may be categorized into four groupings: (1) subsection (a) defines the partnership assets; (2) subsection (b) prescribes the order of payment of liabilities, and subsection (c) gives the order in which assets shall be used to pay the liabilities; (3) subsections (d)-(g) declare rules for contribution from the partners; (4) subsections (h) and (i) prescribe priorities in insolvency situations. Section 40 will be discussed according to this division.

a. *Partnership Assets*.— Assets under section 40 consist of more than the physical property and choses-in-action which the firm may possess on dissolution; they include contributions of the partners which may be required to dispose of liabilities for debts and capital. This is an important concept and a distinct addition to Texas law, since the authors have found no cases dealing with the problem.²⁷³ The rule assumes importance only when the partnership is insolvent; when the firm is solvent at time of dissolution the ordinary firm assets suffice to pay partnership debts (including capital) and no contributions are required.²⁷⁴ The assets are valued as of the date of dissolution both under the act²⁷⁵ and under Texas law.²⁷⁶ Anticipatory profits may not be considered as a firm asset unless they are fairly certain; speculative profits are excluded both by the act and Texas courts.²⁷⁷ Under the act, the partners may of course provide in the partnership agreement that assets shall be valued according to the books at time of dissolution,²⁷⁸ or an arbitrary value may

²⁷² Section 40 is not a cure-all, however. For instance, the act nowhere indicates a method by which complicated accounting problems may be simplified, probably because there is no practical way to do so. The accounting is often formidable when a partnership is dissolved, particularly if the assets and liabilities are considerable or the firm is insolvent. For an illustration of accounting under § 40, see Comment, 23 Rocky Mt. L. Rev. 331 (1951).

²⁷³ Texas of course recognizes a partner's right to seek contribution from his co-partners when he has paid partnership debts, see notes 283-88 *infra* and accompanying text, but this right of an individual partner is not recognized as a firm asset. The act is a recognition of the "entity" theory of partnership; i.e., a partner is a contributor to the partnership. Since debts paid by an individual partner are an advancement, and since advancements must be shared like other losses under § 18(a), the partner's right to get his money returned is unchanged (in all probability) by the act.

²⁷⁴ A more complete explanation of § 40(a) and its significance is in notes 283-88 *infra* and accompanying text.

²⁷⁵ *Froess v. Froess*, 284 Pa. St. 369, 131 Atl. 276 (1925).

²⁷⁶ *Vogt v. Lee*, 32 S.W.2d 688 (Tex. Civ. App. 1930) (semble).

²⁷⁷ *Murray v. Bateman*, 315 Mass. 113, 51 N.E.2d 954 (1943); *Gilleen v. Bennett, Tarlton & Co.*, 264 S.W. 229 (Tex. Civ. App. 1924).

²⁷⁸ *Smith v. Smith*, 307 P.2d 644 (Colo. 1957); *In re Witkino's Estate*, 167 Misc. 885, 4 N.Y.S.2d 933 (1938).

be put upon a partner's interest by an option agreement.²⁷⁹ Texas follows the proposition that final accounting and distribution shall be in accordance with the partnership agreement and books.²⁸⁰

b. *Priority of Liabilities.*—Section 40(b), prescribing how liabilities shall rank in order of payment, adds little to existing Texas law. The act gives preference to partnership debts, which is not remarkable, and then provides that liabilities to partners rank second. After these classes of debts are paid, the partners are entitled to a return of their capital, and the balance remaining, if any, is distributed as profits. Texas is in accord with all of these propositions,²⁸¹ and the adoption of section 40(b) would be no more than a convenient clarification. The real problem in insolvency cases is usually in determining whether money which an individual partner has "contributed" to the partnership was intended to be an advancement or loan (entitling him to preference over the other partners in assets remaining after the debts are paid), or an addition to his capital account.²⁸²

Section 40(c) logically provides that the partnership property shall be exhausted before the contributions of the partners are used to pay firm liabilities.

c. *Contributions.*—It is in subsections (d)-(g) that the act offers some of its most constructive legislation. Briefly, they may be summarized as follows.²⁸³ Section 40(d) places an affirmative duty on a partner to contribute his share of the liabilities as provided for by section 18(a); if any partner is insolvent at the time of dissolution, or refuses to pay and is not subject to process, the other partners must contribute a pro rata share of his liability. Section 40(e) permits an assignee for the benefit of creditors (or any court appointee) to enforce the contributions of section 40(d), and section 40(f) permits a partner to enforce the contribution which another part-

²⁷⁹ Black v. Mylish, 351 Pa. 611, 41 A.2d 731 (1943).

²⁸⁰ Peters v. Brookshire, 143 Tex. 21, 182 S.W.2d 361 (1944).

²⁸¹ Partnership debts must be paid first. Smith v. Wayman, 148 Tex. 318, 224 S.W.2d 211 (1949). A partner who has made advancements other than as a capital contribution is a creditor as to the other partners, Paggi v. Quinn, 179 S.W.2d 789 (Tex. Civ. App. 1944) error ref. w.o.m., thus making him a "secondary" creditor, ranking after third-party partnership creditors. After these two classes of debts are paid, each partner is entitled to his actual capital contribution, or a proportionate part of the remaining capital, Johnston v. Ballard, 83 Tex. 486, 18 S.W. 686 (1892); evidence of unequal capital contributions is sufficient to show that the capital is not to be divided equally on dissolution. Ibid. After capital is repaid, any balance remaining is divided among the partners as profits. Newman v. Newman, 195 S.W.2d 393 (Tex. Civ. App. 1946), aff'd, 145 Tex. 433, 198 S.W.2d 91 (1947); cf. Diamond v. Gust, 206 S.W. 366 (Tex. Civ. App. 1918) error ref. (semble).

²⁸² Cf. Paggi v. Quinn, supra note 281.

²⁸³ For full text see Appendix.

ner has not paid, to the extent of his excess payment under subsection (d). Subsection (g) makes a deceased partner's estate liable for his contributions.

Since section 18(a) has already been examined,²⁸⁴ the first clause of subsection (d) will not be discussed further. The second clause of the subsection is worthy of some consideration, even though on its face it is but a recognition of the well-established principle that partners are jointly and severally liable for partnership debts.²⁸⁵ As was noted above, the right to contribution includes partners' contributions for capital losses, which are in proportion to each partner's share of the profits. This second clause, then, would in the cases of a partner's insolvency or immunity from process force the other partners to share a greater portion of the capital losses. The situation would be novel in Texas jurisprudence; from existing case law it is probable that such a result would not now be reached,²⁸⁶ fair though it may be. The impact of this clause obviously would be greatest on intra-partnership relations.

Creditors' rights in partnership property have already been discussed,²⁸⁷ and no further effort will be made in that direction in connection with section 40(e). This subsection and subsections (f) and (g) merely grant procedural dispensations enabling interested parties to enforce rights previously created.²⁸⁸

d. *Priorities of Creditors Where Partnership Insolvent.*²⁸⁹—The act incorporates into section 40(h) the prevailing rule that partnership creditors have priority in partnership property and separate creditors in individual property. This section, along with section 40(i), which decrees that separate creditors of a partner are preferred over partnership creditors, would materially change existing Texas law; our courts hold that "the holder of a claim

²⁸⁴ For a discussion of § 18(a), see text following note 146 *supra*.

²⁸⁵ Texas has recognized this principle from earliest days. See, e.g., *Smith v. Wayman*, 148 Tex. 318, 224 S.W.2d 211 (1949); *Wiggins v. Blackshear*, 86 Tex. 665, 26 S.W. 939 (1894).

²⁸⁶ This conclusion is reached not because of any particular case, but because of the general confusion in the cases concerning capital losses. See text following note 117 *supra*, discussing the Texas cases dealing with capital losses. See particularly *Bradford v. Bradford*, 172 S.W.2d 365, 367 (Tex. Civ. App. 1943), where the court approved this statement: "The law will not imply a promise by a copartner to repay advancements of capital during the continuance or at the dissolution of the partnership."

²⁸⁷ See note 68 *supra* and following text.

²⁸⁸ No case has been found in which a Texas assignee for the benefit of creditors sought to enforce a partner's right to contributions, although partners have frequently sought contributions. See e.g., *Paggi v. Quinn*, 179 S.W.2d 789 (Tex. Civ. App. 1944) error ref. A partner's individual property would certainly be liable for his contribution. *Ibid*.

²⁸⁹ For a discussion of related material see note 214 *supra*.

against a partnership can establish a claim against the estate of a deceased partner, and *share equally and pro rata with separate creditors*.²⁹⁰ Whether or not this change is desirable,²⁹¹ it would of course bring Texas in line with the rule in the great majority of states.

V. CONCLUSIONS

Partnerships, nearly a million of them, are the commonest form of business association in the United States.²⁹² Texas undoubtedly has the largest number of these not subject to any comprehensive corpus of substantive law. Texas courts have, of course, decided the many cases brought before them. But it is no insult to the courts that they have produced some highly individual results and that the totality of their decisions is in some respects incoherent and in others incomplete; this is the nature of the common law. Our Article has reviewed the cases, demonstrated their defects, and described the cures offered by the Uniform Partnership Act.

The act is a rational distillation of the common law. It is therefore no surprise to find that the act generally harmonizes with Texas cases. Where it differs, it offers improvements. Its uniformity is no mere promise, for it has been adopted in thirty-seven jurisdictions. This in itself is a virtue where interstate enterprise and ownership prevail. It also means that the act has been thoroughly tested and found workable.

The major improvements which the act would accomplish in Texas are:

- (1) Authorizing partnerships to hold and convey title to realty;
- (2) Allowing individual creditors to charge or take assignments of a partner's interest without a dissolution, thus protecting the co-partners;
- (3) Eliminating confusion as to the causes and consequences of dissolution, *e.g.*, by assuring remaining partners the right to wind up, allowing innocent partners the right to buy the interest of a wrongfully dissolving partner, and limiting the notice necessary to prevent the incurring of new liabilities after dissolution;

²⁹⁰ Webb v. Gregory, 108 S.W. 478, 479 (Tex. Civ. App. 1908); see also Higgins v. Rector, 47 Tex. 361 (1877).

²⁹¹ Professor Crane states that the traditional rule is "logically indefensible," since it deprives the partnership creditor of his legal rights against the separate property at the time he needs most to exercise them. Crane, Partnership § 94 (2d ed. 1952).

²⁹² In 1953, the latest year for which figures are available, 958,591 partnerships, compared to 697,975 corporations, filed federal income tax returns. U. S. Treasury Dep't, Internal Revenue Service, Statistics of Income for 1953, Partnership Returns 49 (1957) and Corporation Income Tax Returns 27 (1956).

(4) Preserving the rights of partnership creditors despite a change in members of the firm;

(5) Altering the nature of partnership property in order to preserve prior rights of partnership creditors, *e.g.*, by freeing them from the subrogation of their priority to the partners and of partners (*e.g.*, by preventing a partner from assigning individually his interest in partnership property);

(6) Specifying that the right of contribution is a partnership asset, prescribing in detail the order of priority for distribution of partnership assets.

Among the many lesser improvements of the act are:

(1) Confirming that a corporation may be a partner;²⁹³

(2) Formalizing the mutual agency relationships of partners;²⁹⁴

(3) Permitting an accounting in appropriate instances without dissolution;

(4) Systematizing relations among partners (without removing their right to provide otherwise by contract), *e.g.*, by requiring all losses (including capital losses) to be shared, by extending fiduciary relations, and by eliminating implied agreements for special compensation.

The Uniform Partnership Act goes far toward curing the numerous defects in Texas law. Moreover, the act contains a careful, coherent, and comprehensive body of partnership principles which Texas sadly needs.

²⁹³ § 2 (defining "person" to include corporations) and § 6 (defining "partnership" as an association of two or more persons). The purport of Tex. Bus. Corp. Act. art. 2.02A(7) (1955) may be the same, but its efficacy has not yet been established.

²⁹⁴ § 9. This has not been discussed in the Article since it would not make important changes. Its primary contribution would be to eliminate the unfortunate and artificial limitation on the authority of "non-trading" partners. See *Randall v. Meredith*, 76 Tex. 669, 13 S.W. 576 (1890).

APPENDIX

Uniform Partnership Act

PART I—PRELIMINARY PROVISIONS

§ 1. *Name of Act.*—This act may be cited as Uniform Partnership Act.

§ 2. *Definition of Terms.*—In this act, "Court" includes every court and judge having jurisdiction in the case.

"Business" includes every trade, occupation, or profession.

"Person" includes individuals, partnerships, corporations, and other associations.

"Bankrupt" includes bankrupt under the Federal Bankruptcy Act or insolvent under any state insolvent act.

"Conveyance" includes every assignment, lease, mortgage, or encumbrance.

"Real property" includes land and any interest or estate in land.

§ 3. *Interpretation of Knowledge and Notice.*—(1) A person has "knowledge" of a fact within the meaning of this act not only when he has actual knowledge thereof, but also when he has knowledge of such other facts as in the circumstances shows bad faith.

(2) A person has "notice" of a fact within the meaning of this act when the person who claims the benefit of the notice:

(a) States the fact to such person, or

(b) Delivers through the mail, or by other means of communication, a written statement of the fact to such person or to a proper person at his place of business or residence.

§ 4. *Rules of Construction.*—(1) The rule that statutes in derogation of the common law are to be strictly construed shall have no application to this act.

(2) The law of estoppel shall apply under this act.

(3) The law of agency shall apply under this act.

(4) This act shall be so interpreted and construed as to effect its general purpose to make uniform the law of those states which enact it.

(5) This act shall not be construed so as to impair the obligations of any contract existing when the act goes into effect, nor to affect any action or proceedings begun or right accrued before this act takes effect.

§ 5. *Rules for Cases Not Provided for in This Act.*—In any case not provided for in this act the rules of law and equity, including the law merchant, shall govern.

PART II—NATURE OF A PARTNERSHIP

§ 6. *Partnership Defined.*—(1) A partnership is an association of two or more persons to carry on as co-owners a business for profit.

(2) But any association formed under any other statute of this state, or any statute adopted by authority, other than the authority of this state, is not a partnership under this act, unless such association would have been a partnership in this state prior to the adoption of this act; but this act shall apply to limited partnerships except in so far as the statutes relating to

such partnerships are inconsistent herewith.

§ 7. *Rules for Determining the Existence of a Partnership.*—In determining whether a partnership exists, these rules shall apply:

(1) Except as provided by section 16 persons who are not partners as to each other are not partners as to third persons.

(2) Joint tenancy, tenancy in common, tenancy by the entireties, joint property, common property, or part ownership does not of itself establish a partnership, whether such co-owners do or do not share any profits made by the use of the property.

(3) The sharing of gross returns does not of itself establish a partnership, whether or not the persons sharing them have a joint or common right or interest in any property from which the returns are derived.

(4) The receipt by a person of a share of the profits of a business is prima facie evidence that he is a partner in the business, but no such inference shall be drawn if such profits were received in payment:

(a) As a debt by installments or otherwise,

(b) As wages of an employee or rent to a landlord,

(c) As an annuity to a widow or representative of a deceased partner,

(d) As interest on a loan, though the amount of payment vary with the profits of the business,

(e) As the consideration for the sale of a good-will of a business or other property by installments or otherwise.

§ 8. *Partnership Property.*—(1) All property originally brought into the partnership stock or subsequently acquired by purchase or otherwise, on account of the partnership, is partnership property.

(2) Unless the contrary intention appears, property acquired with partnership funds is partnership property.

(3) Any estate in real property may be acquired in the partnership name. Title so acquired can be conveyed only in the partnership name.

(4) A conveyance to a partnership in the partnership name, though without words of inheritance, passes the entire estate of the grantor unless a contrary intent appears.

PART III—RELATIONS OF PARTNERS TO PERSONS DEALING WITH THE PARTNERSHIP

§ 9. *Partner Agent of Partnership as to Partnership Business.*—(1) Every partner is an agent of the partnership for the purpose of its business, and the act of every partner, including the execution in the partnership name of any instrument, for apparently carrying on in the usual way the business of the partnership of which he is a member binds the partnership, unless the partner so acting has in fact no authority to act for the partnership in the particular matter, and the person with whom he is dealing has knowledge of the fact that he has no such authority.

(2) An act of a partner which is not apparently for the carrying on of the business of the partnership in the usual way does not bind the partnership unless authorized by the other partners.

(3) Unless authorized by the other partners or unless they have abandoned the business, one or more but less than all the partners have no authority to:

(a) Assign the partnership property in trust for creditors or on the assignee's promise to pay the debts of the partnership,

(b) Dispose of the good-will of the business,

(c) Do any other act which would make it impossible to carry on the ordinary business of a partnership,

(d) Confess a judgment,

(e) Submit a partnership claim or liability to arbitration or reference.

(4) No act of a partner in contravention of a restriction on authority shall bind the partnership to persons having knowledge of the restriction.

§ 10. *Conveyance of Real Property of the Partnership.*—(1) Where title to real property is in the partnership name, any partner may convey title to such property by a conveyance executed in the partnership name; but the partnership may recover such property unless the partner's act binds the partnership under the provisions of paragraph (1) of section 9, or unless such property has been conveyed by the grantee or a person claiming through such grantee to a holder for value without knowledge that the partner, in making the conveyance, has exceeded his authority.

(2) Where title to real property is in the name of the partnership, a conveyance executed by a partner, in his own name, passes the equitable interest of the partnership, provided the act is one within the authority of the partner under the provisions of paragraph (1) of section 9.

(3) Where title to real property is in the name of one or more but not all the partners, and the record does not disclose the right of the partnership, the partners in whose name the title stands may convey title to such property, but the partnership may recover such property if the partners' act does not bind the partnership under the provisions of paragraph (1) of section 9, unless the purchaser or his assignee, is a holder for value, without knowledge.

(4) Where the title to real property is in the name of one or more or all the partners, or in a third person in trust for the partnership, a conveyance executed by a partner in the partnership name, or in his own name, passes the equitable interest of the partnership, provided the act is one within the authority of the partner under the provisions of paragraph (1) of section 9.

(5) Where the title to real property is in the names of all the partners a conveyance executed by all the partners passes all their rights in such property.

§ 11. *Partnership Bound by Admission of Partner.*—An admission or representation made by any partner concerning partnership affairs within the scope of his authority as conferred by this act is evidence against the partnership.

§ 12. *Partnership Charged with Knowledge of or Notice to Partner.*—Notice to any partner of any matter relating to partnership affairs, and the knowledge of the partner acting in the particular matter, acquired while a partner or then present to his mind, and the knowledge of any other partner who reasonably could and should have communicated it to the acting partner, operate as notice to or knowledge of the partnership, except in the case of a fraud on the partnership committed by or with the consent of that partner.

§ 13. *Partnership Bound by Partner's Wrongful Act.*—Where, by any wrongful act or omission of any partner acting in the ordinary course of the business of the partnership or with the authority of his co-partners, loss or injury is caused to any person, not being a partner in the partnership, or any penalty is incurred, the partnership is liable therefor to the same extent as the partner so acting or omitting to act.

§ 14. *Partnership Bound by Partner's Breach of Trust.*—The partnership is bound to make good the loss:

(a) Where one partner acting within the scope of his apparent authority receives money or property of a third person and misapplies it; and

(b) Where the partnership in the course of its business receives money or property of a third person and the money or property so received is misapplied by any partner while it is in the custody of the partnership.

§ 15. *Nature of Partner's Liability.*—All partners are liable

(a) Jointly and severally for everything chargeable to the partnership under sections 13 and 14.

(b) Jointly for all other debts and obligations of the partnership; but any partner may enter into a separate obligation to perform a partnership contract.

§ 16. *Partner by Estoppel.*—(1) When a person, by words spoken or written or by conduct, represents himself, or consents to another representing him to any one, as a partner in an existing partnership or with one or more persons not actual partners, he is liable to any such person to whom such representation has been made, who has, on the faith of such representation, given credit to the actual or apparent partnership, and if he has made such representation or consented to its being made in a public manner he is liable to such person, whether the representation has or has not been made or communicated to such person so giving credit by or with the knowledge of the apparent partner making the representation or consenting to its being made.

(a) When a partnership liability results, he is liable as though he were an actual member of the partnership.

(b) When no partnership liability results, he is liable jointly with the other persons, if any, so consenting to the contract or representation as to incur liability, otherwise separately.

(2) When a person has been thus represented to be a partner in an existing partnership, or with one or more persons not actual partners, he is an agent of the persons consenting to such representation to bind them to the same extent and in the same manner as though he were a partner in fact, with respect to persons who rely upon the representation. Where all the members of the existing partnership consent to the representation, a partnership act or obligation results; but in all other cases it is the joint act or obligation of the person acting and the persons consenting to the representation.

§ 17. *Liability of Incoming Partner.*—A person admitted as a partner into an existing partnership is liable for all the obligations of the partnership arising before his admission as though he had been a partner when such obligations were incurred, except that this liability shall be satisfied only out of partnership property.

PART IV — RELATIONS OF PARTNERS TO ONE ANOTHER

§ 18. *Rules Determining Rights and Duties of Partners.*—The rights and duties of the partners in relation to the partnership shall be determined, subject to any agreement between them, by the following rules:

(a) Each partner shall be repaid his contributions, whether by way of capital or advances to the partnership property and share equally in the profits and surplus remaining after all liabilities, including those to partners, are satisfied; and must contribute toward the losses, whether of capital or otherwise, sustained by the partnership according to his share in the profits.

(b) The partnership must indemnify every partner in respect of payments made and personal liabilities reasonably incurred by him in the ordinary and proper conduct of its business, or for the preservation of its business or property.

(c) A partner, who in aid of the partnership makes any payment or advance beyond the amount of capital which he agreed to contribute, shall be paid interest from the date of the payment or advance.

(d) A partner shall receive interest on the capital contributed by him only from the date when repayment should be made.

(e) All partners have equal rights in the management and conduct of the partnership business.

(f) No partner is entitled to remuneration for acting in the partnership business, except that a surviving partner is entitled to reasonable compensation for his services in winding up the partnership affairs.

(g) No person can become a member of a partnership without the consent of all the partners.

(h) Any difference arising as to ordinary matters connected with the partnership business may be decided by a majority of the partners; but no act in contravention of any agreement between the partners may be done rightfully without the consent of all the partners.

§ 19. *Partnership Books.*—The partnership books shall be kept, subject to any agreement between the partners, at the principal place of business of the partnership, and every partner shall at all times have access to and may inspect and copy any of them.

§ 20. *Duty of Partners to Render Information.*—Partners shall render on demand true and full information of all things affecting the partnership to any partner or the legal representative of any deceased partner or partner under legal disability.

§ 21. *Partner Accountable as a Fiduciary.*—(1) Every partner must account to the partnership for any benefit, and hold as trustee for it any profits derived by him without the consent of the other partners from any transaction connected with the formation, conduct, or liquidation of the partnership or from any use by him of its property.

(2) This section applies also to the representatives of a deceased partner engaged in the liquidation of the affairs of the partnership as the personal representatives of the last surviving partner.

§ 22. *Right to an Account.*—Any partner shall have the right to a formal account as to partnership affairs:

- (a) If he is wrongfully excluded from the partnership business or possession of its property by his co-partners,
- (b) If the right exists under the terms of any agreement,
- (c) As provided by section 21,
- (d) Whenever other circumstances render it just and reasonable.

§ 23. *Continuation of Partnership Beyond Fixed Term.*—(1) When a partnership for a fixed term or particular undertaking is continued after the termination of such term or particular undertaking without any express agreement, the rights and duties of the partners remain the same as they were at such termination, so far as is consistent with a partnership at will.

(2) A continuation of the business by the partners or such of them as habitually acted therein during the term, without any settlement or liquidation of the partnership affairs, is prima facie evidence of a continuation of the partnership.

PART V — PROPERTY RIGHTS OF A PARTNER

§ 24. *Extent of Property Rights of a Partner.*—The property rights of a partner are (1) his rights in specific partnership property, (2) his interest in the partnership, and (3) his right to participate in the management.

§ 25. *Nature of a Partner's Right in Specific Partnership Property.*—(1) A partner is co-owner with his partners of specific partnership property holding as a tenant in partnership.

(2) The incidents of this tenancy are such that:

(a) A partner, subject to the provisions of this act and to any agreement between the partners, has an equal right with his partners to possess specific partnership property for partnership purposes; but he has no right to possess such property for any other purpose without the consent of his partners.

(b) A partner's right in specific partnership property is not assignable except in connection with the assignment of rights of all the partners in the same property.

(c) A partner's right in specific partnership property is not subject to attachment or execution, except on a claim against the partnership. When partnership property is attached for a partnership debt the partners, or any of them, or the representatives of a deceased partner, cannot claim any right under the homestead or exemption laws.

(d) On the death of a partner his right in specific partnership property vests in the surviving partner or partners, except where the deceased was the last surviving partner, when his right in such property vests in his legal representative. Such surviving partner or partners, or the legal representative of the last surviving partner, has no right to possess the partnership property for any but a partnership purpose.

(e) A partner's right in specific partnership property is not subject to dower, curtesy, or allowances to widows, heirs, or next of kin.

§ 26. *Nature of Partner's Interest in the Partnership.*—A partner's interest in the partnership is his share of the profits and surplus, and the same is personal property.

§ 27. *Assignment of Partner's Interest.*—(1) A conveyance by a partner of his interest in the partnership does not of itself dissolve the partnership, nor, as against the other partners in the absence of agreement, entitle the assignee, during the continuance of the partnership, to interfere in the management or administration of the partnership business or affairs, or to require any information or account of partnership transactions, or to inspect the partnership books; but it merely entitles the assignee to receive in accordance with his contract the profits to which the assigning partner would otherwise be entitled.

(2) In case of a dissolution of the partnership, the assignee is entitled to receive his assignor's interest and may require an account from the date only of the last account agreed to by all the partners.

§ 28. *Partner's Interest Subject to Charging Order.*—(1) On due application to a competent court by any judgment creditor of a partner, the court which entered the judgment, order, or decree, or any other court, may charge the interest of the debtor partner with payment of the unsatisfied amount of such judgment debt with interest thereon; and may then or later appoint a receiver of his share of the profits, and of any other money due or to fall due to him in respect of the partnership, and make all other orders, directions, accounts and inquiries which the debtor partner might have made, or which the circumstances of the case may require.

(2) The interest charged may be redeemed at any time before foreclosure, or in case of a sale being directed by the court may be purchased without thereby causing a dissolution:

(a) With separate property, by any one or more of the partners, or

(b) With partnership property, by any one or more of the partners with the consent of all the partners whose interests are not so charged or sold.

(3) Nothing in this act shall be held to deprive a partner of his right, if any, under the exemption laws, as regards his interest in the partnership.

PART VI—DISSOLUTION AND WINDING UP

§ 29. *Dissolution Defined.*—The dissolution of a partnership is the change in the relation of the partners caused by any partner ceasing to be associated in the carrying on as distinguished from the winding up of the business.

§ 30. *Partnership Not Terminated by Dissolution.*—On dissolution the partnership is not terminated, but continues until the winding up of partnership affairs is completed.

§ 31. *Causes of Dissolution.*—Dissolution is caused:

(1) Without violation of the agreement between the partners,

(a) By the termination of the definite term or particular undertaking specified in the agreement,

(b) By the express will of any partner when no definite term or particular undertaking is specified,

(c) By the express will of all the partners who have not assigned their interests or suffered them to be charged for their separate debts,

either before or after the termination of any specified term or particular undertaking,

(d) By the expulsion of any partner from the business bona fide in accordance with such a power conferred by the agreement between the partners;

(2) In contravention of the agreement between the partners, where the circumstances do not permit a dissolution under any other provision of this section, by the express will of any partner at any time;

(3) By any event which makes it unlawful for the business of the partnership to be carried on or for the members to carry it on in partnership;

(4) By the death of any partner;

(5) By the bankruptcy of any partner or the partnership;

(6) By decree of court under section 32.

§ 32. *Dissolution by Decree of Court.*—(1) On application by or for a partner the court shall decree a dissolution whenever:

(a) A partner has been declared a lunatic in any judicial proceeding or is shown to be of unsound mind,

(b) A partner becomes in any other way incapable of performing his part of the partnership contract,

(c) A partner has been guilty of such conduct as tends to affect prejudicially the carrying on of the business,

(d) A partner wilfully or persistently commits a breach of the partnership agreement, or otherwise so conducts himself in matters relating to the partnership business that it is not reasonably practicable to carry on the business in partnership with him,

(e) The business of the partnership can only be carried on at a loss,

(f) Other circumstances render a dissolution equitable.

(2) On the application of the purchaser of a partner's interest under sections 27 and 28:

(a) After the termination of the specified term or particular undertaking,

(b) At any time if the partnership was a partnership at will when the interest was assigned or when the charging order was issued.

§ 33. *General Effect of Dissolution on Authority of Partner.*—Except so far as may be necessary to wind up partnership affairs or to complete transactions begun but not then finished, dissolution terminates all authority of any partner to act for the partnership,

(1) With respect to the partners,

(a) When the dissolution is not by the act, bankruptcy or death of a partner; or

(b) When the dissolution is by such act, bankruptcy or death of a partner, in cases where section 34 so requires.

(2) With respect to persons not partners, as declared in section 35.

§ 34. *Right of Partner to Contribution from Co-partners after Dissolution.*—Where the dissolution is caused by the act, death or bankruptcy of a partner, each partner is liable to his co-partners for his share of any liability created by any partner acting for the partnership as if the partnership had not been dissolved unless

(a) The dissolution being by act of any partner, the partner acting for the partnership had knowledge of the dissolution, or

(b) The dissolution being by the death or bankruptcy of a partner, the partner acting for the partnership had knowledge or notice of the death or bankruptcy.

§ 35. *Power of Partner to Bind Partnership to Third Persons after Dissolution.*—(1) After dissolution a partner can bind the partnership except as provided in Paragraph (3).

(a) By any act appropriate for winding up partnership affairs or completing transactions unfinished at dissolution;

(b) By any transaction which would bind the partnership if dissolution had not taken place, provided the other party to the transaction

(I) Had extended credit to the partnership prior to dissolution and had no knowledge or notice of his want of authority; or

(II) Though he had not so extended credit, had nevertheless known of the partnership prior to dissolution, and, having no knowledge or notice of dissolution, the fact of dissolution had not been advertised in a newspaper of general circulation in the place (or in each place if more than one) at which the partnership business was regularly carried on.

(2) The liability of a partner under Paragraph (1b) shall be satisfied out of partnership assets alone when such partner had been prior to dissolution

(a) Unknown as a partner to the person with whom the contract is made; and

(b) So far unknown and inactive in partnership affairs that the business reputation of the partnership could not be said to have been in any degree due to his connection with it.

(3) The partnership is in no case bound by any act of a partner after dissolution

(a) Where the partnership is dissolved because it is unlawful to carry on the business, unless the act is appropriate for winding up partnership affairs; or

(b) Where the partner has become bankrupt; or

(c) Where the partner has no authority to wind up partnership affairs; except by a transaction with one who

(I) Had extended credit to the partnership prior to dissolution and had no knowledge or notice of his want of authority; or

(II) Had not extended credit to the partnership prior to dissolution, and, having no knowledge or notice of his want of authority, the fact of his want of authority has not been advertised in the manner provided for advertising the fact of dissolution in Paragraph (1bII).

(4) Nothing in this section shall affect the liability under section 16 of any person who after dissolution represents himself or consents to another representing him as a partner in a partnership engaged in carrying on business.

§ 36. *Effect of Dissolution on Partner's Existing Liability.*—(1) The dissolution of the partnership does not of itself discharge the existing liability of any partner.

(2) A partner is discharged from any existing liability upon dissolution

of the partnership by an agreement to that effect between himself, the partnership creditor and the person or partnership continuing the business; and such agreement may be inferred from the course of dealing between the creditor having knowledge of the dissolution and the person or partnership continuing the business.

(3) Where a person agrees to assume the existing obligations of a dissolved partnership, the partners whose obligations have been assumed shall be discharged from any liability to any creditor of the partnership who, knowing of the agreement, consents to a material alteration in the nature or time of payment of such obligations.

(4) The individual property of a deceased partner shall be liable for all obligations of the partnership incurred while he was a partner but subject to the prior payment of his separate debts.

§ 37. *Right to Wind Up*.—Unless otherwise agreed the partners who have not wrongfully dissolved the partnership or the legal representative of the last surviving partner, not bankrupt, has the right to wind up the partnership affairs; provided, however, that any partner, his legal representative or his assignee, upon cause shown, may obtain winding up by the court.

§ 38. *Rights of Partners to Application of Partnership Property*.—(1) When dissolution is caused in any way, except in contravention of the partnership agreement, each partner, as against his co-partners and all persons claiming through them in respect of their interests in the partnership, unless otherwise agreed, may have the partnership property applied to discharge its liabilities, and the surplus applied to pay in cash the net amount owing to the respective partners. But if dissolution is caused by expulsion of a partner, bona fide under the partnership agreement and if the expelled partner is discharged from all partnership liabilities, either by payment or agreement under section 36(2), he shall receive in cash only the net amount due him from the partnership.

(2) When dissolution is caused in contravention of the partnership agreement the rights of the partners shall be as follows:

(a) Each partner who has not caused dissolution wrongfully shall have,

(I) All the rights specified in paragraph (1) of this section, and

(II) The right, as against each partner who has caused the dissolution wrongfully, to damages for breach of the agreement.

(b) The partners who have not caused the dissolution wrongfully, if they all desire to continue the business in the same name, either by themselves or jointly with others, may do so, during the agreed term for the partnership and for that purpose may possess the partnership property, provided they secure the payment by bond approved by the court, or pay to any partner who has caused the dissolution wrongfully, the value of his interest in the partnership at the dissolution, less any damages recoverable under clause (2aII) of this section, and in like manner indemnify him against all present or future partnership liabilities.

(c) A partner who has caused the dissolution wrongfully shall have:

(1) If the business is not continued under the provisions of paragraph (2b) all the rights of a partner under paragraph (1), subject to clause (2aII), of this section,

(II) If the business is continued under paragraph (2b) of this section the right as against his co-partners and all claiming through them in respect of their interests in the partnership, to have the value of his interest in the partnership, less any damages caused to his co-partners by the dissolution, ascertained and paid to him in cash, or the payment secured by bond approved by the court, and to be released from all existing liabilities of the partnership; but in ascertaining the value of the partner's interest the value of the good-will of the business shall not be considered.

§ 39. *Rights Where Partnership is Dissolved for Fraud or Misrepresentation.*—Where a partnership contract is rescinded on the ground of the fraud or misrepresentation of one of the parties thereto, the party entitled to rescind is, without prejudice to any other right, entitled,

(a) To a lien on, or right of retention of, the surplus of the partnership property after satisfying the partnership liabilities to third persons for any sum of money paid by him for the purchase of an interest in the partnership and for any capital or advances contributed by him; and

(b) To stand, after all liabilities to third persons have been satisfied, in the place of the creditors of the partnership for any payments made by him in respect of the partnership liabilities; and

(c) To be indemnified by the person guilty of the fraud or making the representation against all debts and liabilities of the partnership.

§ 40. *Rules for Distribution.*—In settling accounts between the partners after dissolution, the following rules shall be observed, subject to any agreement to the contrary:

(a) The assets of the partnership are:

(I) The partnership property,

(II) The contributions of the partners necessary for the payment of all the liabilities specified in clause (b) of this paragraph.

(b) The liabilities of the partnership shall rank in order of payment, as follows:

(I) Those owing to creditors other than partners,

(II) Those owing to partners other than for capital and profits,

(III) Those owing to partners in respect of capital,

(IV) Those owing to partners in respect of profits.

(c) The assets shall be applied in the order of their declaration in clause (a) of this paragraph to the satisfaction of the liabilities.

(d) The partners shall contribute, as provided by section 18(a) the amount necessary to satisfy the liabilities; but if any, but not all, of the partners are insolvent, or, not being subject to process, refuse to contribute, the other partners shall contribute their share of the liabilities, and, in the relative proportions in which they share the profits, the additional amount necessary to pay the liabilities.

(e) An assignee for the benefit of creditors or any person appointed by the court shall have the right to enforce the contributions specified in clause (d) of this paragraph.

(f) Any partner or his legal representative shall have the right to enforce the contributions specified in clause (d) of this paragraph, to the extent of the amount which he has paid in excess of his share of the liability.

(g) The individual property of a deceased partner shall be liable for the contributions specified in clause (d) of this paragraph.

(h) When partnership property and the individual properties of the partners are in possession of a court for distribution, partnership creditors shall have priority on partnership property and separate creditors on individual property, saving the rights of lien or secured creditors as heretofore.

(i) Where a partner has become bankrupt or his estate is insolvent the claims against his separate property shall rank in the following order:

(I) Those owing to separate creditors,

(II) Those owing to partnership creditors,

(III) Those owing to partners by way of contribution.

§ 41. *Liability of Persons Continuing the Business in Certain Cases.*—

(1) When any new partner is admitted into an existing partnership, or when any partner retires and assigns (or the representative of the deceased partner assigns) his rights in partnership property to two or more of the partners, or to one or more of the partners and one or more third persons, if the business is continued without liquidation of the partnership affairs, creditors of the first or dissolved partnership are also creditors of the partnership so continuing the business.

(2) When all but one partner retire and assign (or the representative of a deceased partner assigns) their rights in partnership property to the remaining partner, who continues the business without liquidation of partnership affairs, either alone or with others, creditors of the dissolved partnership are also creditors of the person or partnership so continuing the business.

(3) When any partner retires or dies and the business of the dissolved partnership is continued as set forth in paragraphs (1) and (2) of this section, with the consent of the retired partners or the representative of the deceased partner, but without any assignment of his right in partnership property, rights of creditors of the dissolved partnership and of the creditors of the person or partnership continuing the business shall be as if such assignment had been made.

(4) When all the partners or their representatives assign their rights in partnership property to one or more third persons who promise to pay the debts and who continue the business of the dissolved partnership, creditors of the dissolved partnership are also creditors of the person or partnership continuing the business.

(5) When any partner wrongfully causes a dissolution and the remaining partners continue the business under the provisions of section 38(2b), either alone or with others, and without liquidation of the partnership affairs, creditors of the dissolved partnership are also creditors of the person or partnership continuing the business.

(6) When a partner is expelled and the remaining partners continue the business either alone or with others, without liquidation of the partnership affairs, creditors of the dissolved partnership are also creditors of the person or partnership continuing the business.

(7) The liability of a third person becoming a partner in the partnership continuing the business, under this section, to the creditors of the dissolved partnership shall be satisfied out of partnership property only.

(8) When the business of a partnership after dissolution is continued under any conditions set forth in this section the creditors of the dissolved partnership, as against the separate creditors of the retiring or deceased partner or the representative of the deceased partner, have a prior right to any claim of the retired partner or the representative of the deceased partner against the person or partnership continuing the business, on account of the retired or deceased partner's interest in the dissolved partnership or on account of any consideration promised for such interest or for his right in partnership property.

(9) Nothing in this section shall be held to modify any right of creditors to set aside any assignment on the ground of fraud.

(10) The use by the person or partnership continuing the business of the partnership name, or the name of a deceased partner as part thereof, shall not of itself make the individual property of the deceased partner liable for any debts contracted by such person or partnership.

§ 42. *Rights of Retiring or Estate of Deceased Partner When the Business is Continued.*—When any partner retires or dies, and the business is continued under any of the conditions set forth in section 41 (1, 2, 3, 5, 6), or section 38 (2b), without any settlement of accounts as between him or his estate and the person or partnership continuing the business, unless otherwise agreed, he or his legal representative as against such persons or partnership may have the value of his interest at the date of dissolution ascertained, and shall receive as an ordinary creditor an amount equal to the value of his interest in the dissolved partnership with interest, or, at his option or at the option of his legal representative, in lieu of interest, the profits attributable to the use of his right in the property of the dissolved partnership; provided that the creditors of the dissolved partnership as against the separate creditors, or the representative of the retired or deceased partner, shall have priority on any claim arising under this section, as provided by section 41 (8) of this act.

§ 43. *Accrual of Actions.*—The right to an account of his interest shall accrue to any partner, or his legal representative, as against the winding up partners or the surviving partners or the person or partnership continuing the business, at the date of dissolution, in the absence of any agreement to the contrary.

PART VII — MISCELLANEOUS PROVISIONS

§ 44. *When Act Takes Effect.*—This act shall take effect on the _____ day of _____ one thousand nine hundred and _____.

§ 45. *Legislation Repealed.*—All acts or parts of acts inconsistent with this act are hereby repealed.